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GOVERNMENT EXPENDITURES AND FISCAL

POLICY : AN APPROACH TO ANALYSIS

by

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A THESIS

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The undersigned certify that they have read, and recommend to the Faculty of Graduate Studies for acceptance, a thesis entitled "Government Expenditures and Fiscal Policy : An Approach to Analysis", submitted by John Charles Strick, in partial fulfilment of the requirements for the degree of Doctor of Philosophy.

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ABSTRACT

Federal expenditures in Canada currently amount to approximately one-sixth of the Gross National Product. Because of the magnitude of the expenditures, changes in their level and composition are likely to have significant effects on production, income, and employment in the economy. This thesis is concerned with the possibility of establishing a framework for the analysis of the impact of government expenditures on the economy.

The interrelations between public and private transactions warrant closer attention than they have received in the past, particularly for purposes of facilitating the application of fiscal policy. The Government of Canada has recognized an obligation to promote high levels of employment, price stability, and economic growth in the economy. Fiscal policy is one approach which may be adopted for this purpose and on which the government has placed considerable emphasis in the past. There is appreciable scope for fiscal policy in the sphere of government expenditure. The present government accounts, however, do not permit an analysis to be made of the effects of expenditures on the economy. This factor, together with various financial administrative procedures, tend to impede the effective application of fiscal policy.

A scheme or framework is proposed which would provide information or data relevant to an analysis of the effects of government expenditures on the economy. The scheme basically consists of a program-economic

classification of government expenditure transactions. Expenditures are organized within the framework of the program budget which features the identification of the objectives of government operations and their presentation on the basis of programs and activities. Integrated with this budgetary scheme is an economic character classification of expenditures, which is interrelated with the national accounts of Canada by the use of common concepts and definitions. This framework places government expenditures in the broad perspective of the whole economy and serves to indicate the interaction between government and individual sectors and regions of the economy.

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I

INTRODUCTION

This thesis is concerned with the possibility of establishing a framework for the analysis of the impact of government expenditures on the economy. Because of the magnitude of the expenditures of the Government of Canada, their level and composition and changes in their level and composition prominently affect production, income, and employment in the economy. A framework which would provide the appropriate data for a systematic assessment of these effects would be of particular significance for purposes of facilitating the application of fiscal policy.

A. Fiscal Policy

"Fiscal policy" is a vague term associated with government expenditures and revenues.¹ It has generally come to mean the utilization of government revenues and expenditures to stimulate or control activity in the economy to achieve certain economic objectives.² In the literature on fiscal policy, objectives are expressed

¹ Jesse Burkhead has commented on the term as follows: "The term fiscal policy does not have precise meaning, and there is no clear line to divide fiscal policy from public finance, from monetary policy, or from government economic policy. Neither is there agreement on the kinds of government actions which may properly be labelled as fiscal policy actions....In the United States the widespread academic and popular use of the term was greatly stimulated by the publication of Fiscal Policy and Business Cycles by Professor Alvin H. Hansen." Jesse Burkhead, Government Budgeting (New York: John Wiley and Sons, 1956), p. 60.

² Arthur Smithies and J. K. Butters have given one general

in a variety of forms, but they may be summarized as price stability, high levels of resource utilization, and high and stable rates of economic growth.³

In this study fiscal policy is interpreted as the deliberate adjustment of specific government revenue and expenditure programs for the purpose of achieving high levels of employment and promoting economic growth and development. Virtually all government revenue and expenditure transactions have some effect on the economy in terms of employment, production, etc. and possibly contribute to the achievement of these objectives. But only in those circumstances where programs are deliberately adjusted for the primary purpose of achieving

interpretation of fiscal policy, as the term has been used since the mid 1930's, which is as follows: "Its central concern is with the aggregative effects of government expenditures and taxation on income, production and employment." For their comments and for an account of how doctrine on the subject has evolved, see Arthur Smithies and J. K. Butters (eds.), Readings In Fiscal Policy (Illinois: R. D. Irwin, 1955). In respect to the evolution of fiscal policy, see also Arthur Smithies, "Federal Budgeting and Fiscal Policy", A Survey of Contemporary Economics, ed. Howard S. Ellis (Illinois: R. D. Irwin, 1948), I, pp. 174 - 209.

For one of the pioneering works in the field of fiscal policy and its changing role under the influence of John Maynard Keynes, see Alvin H. Hansen, Fiscal Policy and Business Cycles (New York: W. W. Norton and Co., 1941). Hansen considered fiscal policy in the very broad terms of the total expenditure and revenue program of government (ie. on the basis of the multiplier principle any volume of government expenditure, for whatever purpose it was undertaken, would have a "pump primer" effect on a depressed economy and would constitute fiscal policy.)

³The literature on fiscal policy and its objectives and means of achievement is voluminous. See, for example, Gerhard Colm, Essays in Public Finance and Fiscal Policy (New York: Oxford University Press, 1955); C. A. Hall, Fiscal Policy For Stable Growth (New York: Holt, Rinehart and Winston, 1960); Bent Hansen, The Economic Theory of Fiscal Policy (London: George Allen and Urwin, Ltd., 1958); N. F. Keiser, Macroeconomics, Fiscal Policy, and Economic Growth (New York: John Wiley and Sons, 1964); James A. Maxwell, Fiscal Policy (New York: Henry Holt and Co., 1955); M. F. Millikan (ed.), Income Stabilization For a Developing Democracy (New Haven: Yale University Press, 1953); K. E. Poole, Fiscal Policies and The American Economy (New York: Prentice-Hall, 1951); Paul J. Strayer, Fiscal Policy and Politics (New York: Harper and Bros., 1958).

these objectives are they deemed to constitute fiscal policy.⁴ In striving to attain these goals, however, consideration must also be given to price stabilization. Reasonably stable prices will therefore be considered another, though secondary, objective of fiscal policy. Since this study is primarily concerned with government expenditures, the application of the term fiscal policy is further limited to expenditure programs through much of it.

In general, economic growth and high levels of employment are complementary objectives. If a high level of employment is maintained, economic growth, the increase in real product over time,⁵ will automatically occur as long as the labour force is expanding and productivity is being maintained or is increasing. On the other hand, if economic activity is increasing in terms of industrial expansion and the production of goods and services, employment will be increased in the process, for employment and production move more or less in consonance.⁶

⁴The confinement of the term fiscal policy only to those specific actions in respect to government revenues and expenditures which are deliberately undertaken to achieve established economic objectives is in keeping with Jesse Burkhead's interpretation of fiscal policy. Burkhead has interpreted fiscal policy as follows: "Certain kinds of governmental programs are undertaken primarily with a view to their influence on the level of income and employment. Others are modified because of their probable influence on the level of income and employment. Only in those circumstances where government programs are designed or modified in accordance with their effects on these aggregates should they be termed a part of fiscal policy." See Burkhead, op. cit., p. 69.

⁵Economic growth may also be defined as increasing real product or income per capita over time, or it may be expressed in terms of real output per person employed or real output per man-hour.

⁶If output is represented by Y, and inputs of labour and capital are represented by L and K respectively, the aggregate

Assuming that there is no sudden major change in the labour-to-output ratio,⁷ the rate of economic growth will be relatively stable if the rate of population growth is stable and a high level of employment is maintained. A high level of employment will act as a constraint on the rate of economic growth, for it will not be possible for the rate of growth to be greater than the increase in the labour force allows.⁸ Under these conditions the attainment of the objectives of employment, economic growth, and stable prices will therefore preclude any violent fluctuations in the

production function can be expressed as $Y = f(L, K)$. Technological change can result in an increase in the output associated with a given set of inputs, or there may be an increase in the use of capital which would result in increased production with the level of labour employment remaining constant. Alternatively, given the techniques of production, and given the capital stock, output is a direct function of employment. In the short run, techniques and capital stock can be expected to remain fairly constant. Generally, however, as production increases over time, total inputs of both labour and capital will be increased. See Gardner Ackley, Macroeconomic Theory (New York: MacMillan, 1961), pp. 92 - 99.

For a graphic illustration of short-run movements in production and employment for the period 1909 - 49 showing that they move in consonance over the business cycle, see Alvin H. Hansen, Business Cycles and National Income (Expanded Edition; New York: Norton & Co., 1964), p. 5.

⁷It is not meant to imply here that the labour-to-output ratio is constant. In Canada the output per man has doubled in the period 1928 - 63. For an account of changing labour productivity in Canada in terms of total net output to labour input, see Economic Council of Canada, First Annual Review, Economic Goals for Canada to 1970 (Ottawa: Queen's Printer, 1964), pp. 42 - 46; and B. J. Drabble, Potential Output 1946 - 1970, Staff Study No. 2 prepared for the Economic Council of Canada (Ottawa: Queen's Printer, 1965).

⁸See growth models in R. F. Harrod, Towards a Dynamic Economics (London: MacMillan, 1949), and J. R. Hicks, Contribution to the Theory of the Trade Cycle (New York: Oxford University Press, 1950).

levels of production and income.

The condition of a relatively stable labour-to-output ratio, however, is not likely to hold true. There may be periods of rapid technological progress which may result in deviations from the growth trend even as high levels of employment are being maintained. Increased productivity resulting from technical progress and increases in capital intensity in production will raise the high-employment level of production above what it otherwise would have been.⁹

Even under the assumption of a stable labour-to-output ratio there will still be a possibility of fluctuations in production to a certain extent. Unemployment may on occasion fluctuate between the level established as the goal to be achieved and lower levels. The primary concern when upswings in production and income occur as a result of technological progress, increased investment, or greater employment, however, is to prevent a downturn of a magnitude that would cause unemployment to rise above the level established as the objective, or which would result in relative economic stagnation.

⁹For a discussion of technological change and economic growth, see Gardner Ackley, Macroeconomic Theory (New York: MacMillan, 1961), pp. 549 - 553.

R. M. Solow has made a study of the influence of technical change and capital on growth. According to his calculations gross output per man hour has doubled in the United States during the period 1909 - 49 and 87½ percent of the increase is attributable to technical change. The remaining 12½ percent is due to the increased use of capital. See R. M. Solow, "Technical Change and the Aggregate Production Function," Review of Economics and Statistics, XXXIX (August, 1957), pp. 312 - 320. For a similar study, see M. C. Urquhart, "Capital Accumulation, Technical Change and Economic Growth," Canadian Journal of Economics and Political Science, XXV (November, 1959), pp. 411 - 430.

In defining the fiscal goals of high levels of employment, economic growth, and price stability, consideration is given to the need for the reconciliation of these goals.

A high level of employment does not necessarily imply 100 percent employment of the labour force. In a dynamic and growing economy there will no doubt always be a certain amount of unavoidable frictional unemployment. In fact, such an economy requires a certain degree of mobility of labour. Not only is it difficult to maintain 100 percent full employment or a situation in which there are more vacant jobs than unemployed workers, but such a policy would be difficult to reconcile with the objective of maintaining reasonably stable prices. Policy of this nature would aggravate inflationary tendencies, for as the full employment level is approached scarcity of particular types of labour and scarcity of labour in general would lead to increased wages and cost-push inflation. For the purposes of this study a high level of employment means that approximately 97 percent of the labour force is employed.¹⁰

In regard to the objective of economic growth it is difficult to define a "desirable" rate of growth in absolute or relative terms. A desirable growth rate would be one which

¹⁰The Economic Council of Canada has established a three percent rate of unemployment of the labour force as a "realistic objective to be aimed at" See Economic Council of Canada, First Annual Report, Economic Goals for Canada to 1970 (Ottawa: Queen's Printer, 1964), pp. 37 - 42.

results in the employment of available resources and which leads to productivity increases and increases in real income per capita. In addition to satisfying these conditions, the rate of growth should be an equilibrium one. Very rapid rates of growth are difficult to maintain. Growth depends on technological progress and increases in investment. Investment, however, is a rather unsteady component of aggregate expenditure. To the extent that it is, attempts to attain a high rate of growth by increasing investment relative to consumption may lead to a situation in which it would be more difficult to maintain economic stability.

The Economic Council of Canada, on the basis of projections of growth of the labour force and calculations of productivity and employment potentials, has estimated that Canada will require an average annual increase of 5.5 percent in the production of goods and services to the year 1970.¹¹ This rate of growth is kept in mind as a goal of fiscal policy for the overall economy in this study. But in addition to an overall growth rate there is also the problem of regional growth and development, particularly in depressed areas and sectors. Such areas are of primary concern in this study in respect to fiscal policy for economic growth.

The government may apply expenditure policy directly or indirectly to achieve the above fiscal goals. It may employ resources or purchase materials directly for productive purposes which will generate income, production, and employment through the multiplier process. It may also undertake various projects for the purpose of providing social capital which may lead to the

¹¹ Ibid., pp. 46 - 53.

establishment of new industry as a result of the external economies provided. The government may alternatively attempt to stimulate employment and growth indirectly by inducing increased private consumption and investment through grants of funds. It can increase the amount of purchasing power in the hands of the public through various transfer payments which may result in an increased demand for goods and services. Or it may provide subsidies and credit to industry for capital expansion and increased production.

The achievement of the goals of fiscal policy is only one of three generally recognized functions of government budgetary policy. Beside fiscal policy there are also the functions, as R. A. Musgrave describes them, of securing "adjustments in the allocation of resources" and "adjustments in the distribution of income and wealth."¹² Generally, when objectives of fiscal policy are put forth, the implicit assumption is that these other goals of budgetary policy relating to resource allocation and income distribution have been achieved or are in the process of being achieved.¹³

Adjustments in the allocation of resources are frequently required to assist market forces in securing more optimal results. To leave everything to the market mechanism generally results in inefficient resource allocation which leads to the satisfaction of a lower level of private wants, and consequently less social

¹²R. A. Musgrave, The Theory of Public Finance (New York: McGraw-Hill, 1959), p. 5.

¹³Musgrave, in his discussion of fiscal policy, makes the explicit assumption that other objectives of budgetary policy have been achieved when he sets out fiscal policy goals and the means of achieving these goals. See Ibid., pp. 22 - 27.

welfare, than would be possible under a more optimal allocation. Government corrective action is desirable to secure more efficient resource allocation in such situations as monopoly control, decreasing cost conditions, and external economies and diseconomies.¹⁴ Government action is also required for satisfying public wants. These may consist of wants which the market is unable to satisfy as a result of private enterprise being unwilling or unable to provide the goods and services involved. In general, such services cannot be priced and charged for through the market (eg. defence, justice, sanitation) as they "contribute to the welfare of the whole community."¹⁵ Therefore, the government diverts resources for the provision of these goods and services and provides them free of direct charge to the users. But such wants are extensive whereas there are generally various forces present which place limitations on the amount of resources available for government use at any given time. The determination of social wants and the extent to which they are satisfied is essentially a political process. The choice of alternative uses of resources in satisfying these wants is a budgetary process in which quantitative data and economic analysis can figure quite prominently. In the process

¹⁴Ibid., pp. 6 - 7.

¹⁵Ibid., p. 9. Musgrave has termed the wants satisfied by such services as "social wants". Other types of wants satisfied by government action are termed "merit wants". They involve goods and services that the market could provide if consumers chose to purchase them rather than spend their money on other things. Government action is consequently undertaken to "correct individual choice". See Ibid., pp. 9 - 15.

of budgetary decision-making the consideration of the total gains and costs of alternative uses of resources may play a prominent role in making the most efficient use of the resources at the government's disposal.

Adjustments in the distribution of income and wealth are generally undertaken through the tax and transfer system of the budget. There is, however, wide disagreement regarding the "proper" state of distribution.¹⁶

While considerations other than fiscal policy enter budgetary decisions concerning expenditures, all government activities, as was indicated earlier, have an effect on the economy in terms of employment, prices, income, and production. To the extent that they do, government expenditure activities undertaken primarily for purposes of adjustment in resource allocation and distribution of income may contribute to, or may impede, the achievement of fiscal goals. The question is not whether such effects occur, but one of their nature, direction, and significance. The process of formulating fiscal policy measures consists of analyzing the effects of all existing and proposed expenditure policies and programs and, in the light of these effects and the prevailing or forecast conditions in the economy, adjusting expenditures and proposing measures specifically for the achievement of the established fiscal objectives. This requires

¹⁶For a discussion of equity in the distribution of income, see Musgrave, op. cit., pp. 17 - 20; E. D. Allen and O. H. Brownlee, Economics of Public Finance (New York: Prentice-Hall, 1947), pp. 15 - 16; and John F. Due, Government Finance (Illinois: R. D. Irwin, 1959), pp. 9 - 10.

a thorough examination and evaluation of all individual expenditure programs from the point of view of their probable effects on output, employment, and prices and consequently their contribution to the achievement of fiscal policy objectives.

Essentially a process of expenditure analysis is required which will take into consideration the economic impact of expenditures in conjunction with other considerations such as their value in securing adjustments in resource allocation. Such a process would not only facilitate the determination of the impact of expenditures on employment, production, etc., but would also provide the framework for the reconciliation of fiscal policy objectives with the other principal functions of budgetary policy. In fact, a comprehensive objective appraisal of an expenditure program, including repercussion or spillover effects, for purposes of establishing priorities in respect to resource allocation would of necessity appear to take into consideration certain effects of the program which would also be considered from the point of view of fiscal policy. For instance, a navigation project designed to secure an adjustment in resource allocation in the way of providing transportation facilities to the public may, in addition to its direct transportation benefits, cause an increase in the production of established industries and may encourage formation of new industries in the private sector in the area served by the navigation system. The project would achieve the desired results in respect to resource allocation and at the same time contribute to the fiscal goal of economic development. Direct and indirect benefits of the project would be taken into consideration if a comprehensive

cost-benefit analysis is employed in the evaluation of the project from the point of view of resource allocation and public needs.

The extent to which this analysis would yield information relevant to the assessment of the contribution of the project to fiscal goals depends on the chain of effects pursued on the benefit side.¹⁷

Appropriate criteria for determining priorities among expenditure programs providing for the satisfaction of public wants and securing adjustments in resource allocation may take the form of cost-benefit ratios, maximum net value, etc. Criteria for programs constituting fiscal policy are more difficult to establish, although the attributes of such programs are suggested in the established goals of fiscal policy. The goals of high levels of employment and high rates of economic growth imply that government programs directed to these purposes should have considerable employment content, produce spending effects primarily in designated regions and industrial sectors, and should generate external economies.

¹⁷For an account of cost-benefit analysis and the extent to which indirect or repercussion effects may be taken into consideration in such analysis, see W. R. Sewell et al, Guide to Benefit-Cost Analysis (Ottawa: Queen's Printer, 1962); Otto Eckstein, Water-Resource Development. The Economics of Project Evaluation (Cambridge: Harvard University Press, 1961); Otto Eckstein, "A Survey of the Theory of Public Expenditure Criteria", Public Finances: Needs Sources and Utilization, Report of the National Bureau of Economic Research (Princeton: Princeton University Press, 1961), pp. 463 - 468; R. N. McKean, Efficiency In Government Through Systems Analysis (New York: Wiley & Sons, 1958); Jan Tinbergen, "The Appraisal of Road Construction: Two Calculated Schemes", Review of Economics and Statistics, XXXIX (August, 1957), pp. 241 - 249. Tinbergen's model estimates benefits of transportation projects by measuring the change in national income as a result of the projects. It allows for repercussion effects in terms of the total increase in production and income rather than merely considering benefits in the form of savings in transportation costs as is the case in some of the more conventional cost-benefit analysis.

But one of the implicit requirements of programs constituting fiscal policy is that they be justifiable from the point of view of the objective of resource allocation or at least contribute to the achievement of this objective. The use of employment - expenditure ratios as criteria without regard to other aspects of a program is undesirable, for activities which amount to nothing more than digging holes and filling them up again would receive priority on the basis of a high employment content in relation to the amount expended. Criteria for fiscal programs, however, could perhaps take the form of cost-benefit ratios with certain adjustments made to conventional cost-benefit analysis. In the analysis of the benefits of alternative fiscal projects, special consideration could be given to such effects as the employment created by a project in areas of unemployment as well as to other effects. For instance, since there is no opportunity cost of labour if previously unemployed labour is hired, the cost of employing labour could be excluded in the compilation of costs. This would result in lower costs than would otherwise be the case and consequently in a higher ratio of benefits to costs of any project undertaken in areas of unemployment. Or certain weights could be given on the benefit side to such effects as the employment of otherwise unemployed labour. If primary and secondary benefits are analyzed under the conventional cost-benefit method, additional weights could be given to those benefits of a program which correspond to effects predetermined as desirable in terms of generating and inducing employment, production, and income in designated regions and industrial sectors. On this basis, other things being equal, preference would be given to

those fiscal projects which have the most significant impact on employment and production.

B. Analysis of the Impact of Government

Expenditures on the Economy

Program and Spending Effects

Government expenditures may have both spending and program effects on the economy.¹⁸ The spending effect, which may be direct or indirect or both, consists of the immediate or short-term effect on income, production, employment, and prices resulting from direct purchases by government of labour and materials, and from its transfer and subsidy payments and the consequent respending of these funds by recipients. The program effect encompasses the consequences of the existence of the asset which the expenditure program is designed to create. For example, the existence of a new road or dam may encourage the development of, and influence the location of, new industries in the private sector. These would be program effects. The construction industry, however, might expand capacity in order to undertake the construction of the road or dam. This would be a spending effect.

¹⁸The terms "spending effect" and "program effect" are borrowed from Gerhard Colm. He has interpreted these terms as follows: "The spending effect consists of the additional purchasing power created by government expenditures and put into the hands of consumers or business ... The program effect ... takes place not while the money is being spent, but usually after the government project has been completed." See United States, Congress, Senate, Joint Economic Committee, Federal Expenditure Policy for Economic Growth and Stability, Papers Submitted by Panelists Appearing Before the Subcommittee on Fiscal Policy (Washington: Government Printing Office, 1957), p. 434.

Both types of effects are relevant to fiscal policy.

Spending effects may be significant in compensating for temporary maladjustments in economic activity which lead to unemployment. Program effects are likely to contribute to economic growth in the long run and consequently to the achievement of a high level of employment and production in the future.

All government expenditures have a spending effect on the economy. But there remains the question of the significance and direction of this effect. The determination of the spending effect of those governmental programs of an operational or construction nature which, in addition to the resources in the permanent employ of the government, require as inputs the products and services of other industries, necessitates a quantitative analysis of the type and quantity of all materials and services utilized directly, and of the resources required for their production. This type of analysis of proposed government programs would disclose their relation to the various industrial sectors of the economy and would serve to indicate their effect on any temporary imbalances which may exist in these sectors. A depressed industry or region may be stimulated by government demand and by private demand created indirectly as a result of the government expenditure. Alternatively, as the economy approaches the full employment ceiling, strains may be placed on specific areas of the productive system generating an upward pressure on prices. An analysis of government expenditure programs from the point of view of their spending effects would be of value to government in cutting or postponing those programs which would add

significantly to these strains. The effectiveness of fiscal policy in maintaining high levels of employment without contributing to inflationary pressures depends on the government's ability to employ or free the right resources in the appropriate period. Strains on productive capacity and the availability of resources, or alternatively, imbalances resulting in unemployment, may not prevail throughout the entire productive system in any given period. In such circumstances an analysis of the effect of aggregate government expenditures on economic activity as a whole may not be very meaningful. What is required is an analysis of individual government programs and activities from the point of view of their impact on each industrial and regional sector of the economy.

For purposes of analyzing the spending effects of expenditures of the nature of transfer payments, an identification is required of the groups and organizations which are the direct beneficiaries together with an identification of the character of the payment. This would indicate the effect on the incomes of various groups. The indirect effects that may possibly result when the funds are respent by the recipients could be analyzed both on a general basis through the calculation of a multiplier and, where possible, on a more specific basis in terms of other groups, organizations, and sectors affected (e.g. conditional grants to other levels of government, transfers to capital account of industry.)

The government participates in many forms of expenditure operations, but only certain expenditure programs may have a program

effect on economic growth. To the extent that expenditure policies or programs may contribute to the attainment of this objective, it is desirable that in the process of planning programs consideration be given to their possible effects on growth. While it may indeed be difficult to make a precise analysis or evaluation of the total program effects of a government expenditure proposal, a step may be taken towards facilitating an evaluation by, as Colm has suggested, "providing decision makers with an effective approach to program determination."¹⁹

C. Thesis Objective

The objective of this thesis is two-fold. First, it is intended to examine the significance of federal expenditures in Canada as an area for fiscal policy, and to scrutinize the present budgetary system from the point of view of the analysis of the impact of government expenditures on the economy and fiscal policy implementation. Second, a scheme or framework is suggested to provide information or data relevant to a systematic analysis of the spending and program effects of specific expenditure programs. Such a scheme would facilitate the application of fiscal policy.

The procedure followed in conforming to the above objective will be to survey briefly the problems of fiscal policy utilization in a federal system of government. The character and pattern of federal expenditures and provincial and municipal expenditures will be examined to determine the scope for fiscal policy in the area of

¹⁹ Ibid., p. 436.

federal expenditures. A brief analysis will also be made of the attitude of the Canadian government in the past towards employing expenditures for purposes of achieving economic objectives.

Chapter III consists of a description and evaluation of the present budgetary system in Canada regarding expenditure analysis and fiscal policy implementation. An attempt is made to determine to what extent the economic impact of expenditures, that is, the spending and program effects, is taken into consideration in the process of budgeting, the methods of analysis, and some of the problems (e.g. accounting, administrative, political) which impose limitations on the employment of fiscal policy.

The Royal Commission on Government Organization in Canada has recommended a change in organization and procedures concerning budgeting at the federal level, and the Canadian government is presently experimenting with the Commission's recommendations. The program budget which the Commission has proposed may have certain features which may be relevant for expenditure determination and analysis from the point of view of fiscal policy. Chapter IV is devoted to brief evaluation of program budgeting in this respect.

Chapter V consists of a suggested scheme for analyzing the program and spending effects of government expenditures. It concentrates on the form of expenditure accounts required to produce relevant data for the quantitative assessment of these effects and the manner in which such data may be utilized in the analysis of the various types of expenditures. Certain administrat-

ive procedures are considered in brief, particularly the role of the Department of Finance and the Treasury Board, in the analysis of government expenditures and their economic impact. Other implications of this scheme for fiscal policy employment are also examined.

Chapter VI outlines the present attitude of the government towards program budgeting and the need for a system of accounts which would provide the framework for the analysis of the impact of government expenditures on the economy.

II

FISCAL POLICY IN CANADA

To what extent may the expenditures of the federal government be actively and effectively employed for the purpose of achieving fiscal goals? Canada is a federal state and this leads to complications in the application of fiscal policy. Some federal functions are not very appropriate for counter-cyclical or growth policy. Provincial and municipal policies may counter federal ones. Important factors affecting fiscal policy in the sphere of federal expenditures are the responsibilities of the various levels of government, the amounts expended for various functions by each level, intergovernmental transfers, and changing patterns in the composition of expenditures within and between governments. In addition, even though adequate scope for fiscal policy may exist in the area of federal expenditures, there must be a willingness on the part of the federal government to apply expenditures to this purpose.

A. Problems of Fiscal Policy In The Canadian Federal System

The limitations and difficulties of employing fiscal policy in Canada as a result of the federal structure of government have been given considerable attention.¹ The problems arise chiefly

¹See, for example, Canada The Royal Commission on Canada's Economic Prospects, Final Report (Ottawa: Queen's Printer, 1957),

because of the distribution of legislative powers between the federal government and the provincial governments as enumerated and interpreted under the British North America Act.² Each of the two levels of government is sovereign in its own sphere, and the provincial governments are very sensitive to any seeming encroachment by the federal government on areas under their jurisdiction. As a result of this division of jurisdiction the areas in which the government can influence the economy through expenditure policy appear to be limited. Furthermore, provincial and municipal operations may conflict with the objectives of federal fiscal measures:

Although the federal government can bring pressure to bear, it has no power to require the provincial governments to vary the levels of their income and expenditure . . . Because of the federal structure the leverage which the central government can exert on the economy is thus less than it otherwise might be . . . the provincial and municipal governments . . . [are] . . . free to go their own way without regard for counter-cyclical considerations.³

pp. 421 - 432; K. W. Taylor, "Fiscal Policy and Economic Growth", Economics: Canada, ed. M. H. Watkins and D. F. Forster (Toronto: McGraw-Hill, 1964), pp. 161 - 167; J. Stephan Dupre, "The Political Economy of Federal Finance," Economics: Canada, pp. 299 - 312; Canada Tax Foundation, Report of Proceedings of the Eighteenth Annual Tax Conference (Toronto, 1965), pp. 209 - 230; W. C. Hood, "Economic Policy in Our Federal State," Canadian Tax Journal, XII (Nov. - Dec., 1964), pp. 389 - 397; A. W. Johnson and J. M. Andrews, "The Basis and Effects of Provincial-Municipal Fiscal Decisions," Inter-Government Fiscal Relationships, (Canadian Tax Foundation, 1964), pp. 35 - 77; T. N. Brewis et al, Canadian Economic Policy (Toronto: MacMillan Co., 1961), pp. 218 - 229.

²For an appraisal of this distribution, see Canada, Report of the Royal Commission on Dominion-Provincial Relations (Ottawa: Queen's Printer, 1940), Book I, pp. 247 - 259, Book II, pp. 15 - 44.

³T. N. Brewis et al, Canadian Economic Policy (Toronto: MacMillan Co., 1961) p. 226.

The objective of fiscal policy has increased the need for co-operation and co-ordination of policies at all levels of government. The need for co-operation was emphasized in the White Paper on employment and income⁴ in 1945 at a time when the size of the federal government relative to the provincial and municipal governments was so large as to make the operations of the latter appear insignificant.⁵ In the years following the Second World War, as Table II - I illustrates, there has been a shift in the relative amounts expended by the three levels of government in respect to total government expenditure and Gross National Product. This trend has added to the complexity and problems of fiscal policy utilization.

While federal government expenditure has been increasing in absolute terms since the reconversion period following the war, since the mid 1950's it has been decreasing as a percentage of the total expenditures of the three levels of government. As a percentage of Gross National Product it has remained fairly stable. In contrast, the expenditures of the provincial and municipal governments have increased substantially both as a percentage of total government expenditure and as a percentage of Gross National Product. In 1956 provincial-municipal expenditures amounted to

⁴Canada, Department of Reconstruction, Employment and Income (Ottawa: Queen's Printer, 1945).

⁵In 1945 the federal government accounted for over four-fifths of total government expenditure.

TABLE II - I

TOTAL GOVERNMENT EXPENDITURES

(National Accounts basis for selected years in \$ million)

Level of Government	Expenditure			
	1945	1950	1956	1963
Federal	4,272	2,330	5,034	7,432
Federal ^a	4,115	2,079	4,549	6,267
Provincial ^a	441	1,005	1,651	3,574
Municipal ^a	<u>420</u>	<u>898</u>	<u>1,789</u>	<u>3,791</u>
Total ^a	<u>4,976</u>	<u>3,982</u>	<u>7,989</u>	<u>13,632</u>
As % of Total				
Federal	86	58	63	54
Federal ^a	83	52	57	46
Provincial ^a	9	25	20	26
Municipal ^a	<u>8</u>	<u>23</u>	<u>23</u>	<u>28</u>
Total ^a	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>
As % of G.N.P.				
Federal	36.1	12.9	16.5	17.3
Federal ^a	34.8	11.5	14.9	14.6
Provincial ^a	3.7	5.6	5.4	8.3
Municipal ^a	<u>3.5</u>	<u>5.0</u>	<u>5.9</u>	<u>8.8</u>
Total ^a	<u>42.0</u>	<u>22.1</u>	<u>26.2</u>	<u>31.7</u>

^aExcluding inter-governmental transfers. The transfers from one government to another are shown as expenditures on goods and

43 percent of the total government expenditure of \$7,989 million calculated on the National Accounts basis and excluding inter-governmental transfers.⁶ By 1963 this had risen to 54 percent of a total of \$13,632 million. The combined provincial-municipal expenditure as a percentage of Gross National Product increased from 11.3 percent to 17.1 percent in the period 1956 - 63.⁷ As this trend continues and provincial-municipal operations in the economy become increasingly significant, it is apparent that close co-operation between the various levels of government will become necessary if Canada is to have effective fiscal policies.

B. Pattern and Composition of Government

Expenditures in Canada

National Accounts Exposition

Table II - II sets out the pattern of government expenditure by major economic category for the federal and the provincial-municipal governments. These expenditures are on the basis of the National Accounts and are shown as percentages of Gross National

services and as transfers payments to individuals by the recipient governments. SOURCE: Canada, Dominion Bureau of Statistics, National Accounts, Income and Expenditure, 1926 - 56, 1961, and 1963.

⁶For a brief explanation of the difference between government expenditures on the Public Accounts basis and on the National Accounts basis, see Appendix A.

⁷For a similar study of trends in Canadian public finance, see E. J. Hanson, The Public Finance Aspects of Health Services in Canada, Study for the Royal Commission on Health Services (Ottawa: Queen's Printer, 1963), pp. 7 - 17.

TABLE II - II

GOVERNMENT EXPENDITURE BY MAJOR ECONOMIC
CATEGORY AS PERCENTAGE OF GROSS NATIONAL PRODUCT^a

(National Accounts basis for selected years)

Economic Category and Level of Government	1950	1956	1963
Goods and Services	13.0	17.6	18.8
Federal	5.4	8.8	6.8
Provincial-Municipal	7.6	8.8	12.0
Transfer Payments and Subsidies	11.5	11.3	18.3
Federal	7.5	7.7	10.5
Provincial-Municipal	<u>4.0</u>	<u>3.6</u>	<u>7.8</u>
Total Expenditure	24.5	28.9	37.1

^a Includes intergovernmental transfers.

SOURCE: Dominion Bureau of Statistics, National Accounts, Income and Expenditure, 1926 - 56, 1961 and 1963, See Appendix B, Table B-I.

Product. Total government expenditures on goods and services and on transfer payments and subsidies as a percentage of Gross National Product have been increasing over the period 1950 - 63. Federal expenditures on goods and services, however, have been declining over the latter part of this period in relation to Gross National Product, whereas provincial-municipal expenditures have increased by about 50 percent.

Federal and Provincial-Municipal Expenditures:

A Comparison by Function

Table II - III presents a comparison of the net expenditures of federal and provincial-municipal governments on the basis of functions for the fiscal year 1961 - 62. In this table grants-in-aid and shared-cost contributions and payments of a similar nature are excluded from the expenditures of the receiving government and are included in the expenditures of the contributing government in the appropriate function of expenditure.⁸ The federal government is exclusively responsible for defence and veterans' pensions. In regard to other functions, federal government expenditures formed 82 percent of the total government expenditure on social welfare

⁸The data in this table are based on the financial statistics on government expenditure as compiled by the Public Finance and Transportation Division of the Dominion Bureau of Statistics. In the Dominion Bureau of Statistics net figures, conditional grants are included in the expenditure of the paying government only. In regard to federal expenditures, all expenditures which are excluded from "budgetary" expenditure in the Public Accounts of Canada are included, (i.e., expenditures of administrative and special funds, etc.). For an account of the manner in which the Dominion Bureau of Statistics compiles these statistics, see Dominion Bureau of Statistics, A Consolidation of Public Finance Statistics, 1961, (Ottawa: Queen's Printer, 1964).

TABLE II - III

NET EXPENDITURE OF ALL GOVERNMENTS BY
FUNCTION EXCLUDING INTERGOVERNMENTAL TRANSFERS, 1961 - 62

(In Percentage Terms)

Function	<u>% of Amount Expended</u>	
	Federal	Provincial- Municipal
Defence Services and Mutual Aid	100	-
Veterans' Pensions and Other Benefits	100	-
Health, including hospital care	35	65
Social Welfare	82	18
Education	5	95
Transportation and Communications	30	70
Natural Resources and Primary Industries	67	33
Debt Charges	78	22
Contributions to Government Enterprises	88	12
General Government	50	50
Protection of Persons and Property	18	82
Other	<u>51</u>	<u>49</u>
Total Net Expenditure	54	46

SOURCE: Dominion Bureau of Statistics, A Consolidation of Public Finance Statistics, 1961. See Appendix B, Table B - II.

services, 67 percent of the total expended on developing natural resources and primary industries, and 30 percent of the total expended on transportation and communication. In the fields of health, education, transportation and communications, and the protection of persons and property, the combined expenditures of the provinces and municipalities far exceed those of the federal government.

C. Federal Government Expenditures

Data on federal expenditures may be shown on a national accounts basis, in the form of the Dominion Bureau of Statistics compilations as illustrated in Table II - III and Appendix B, Table B - II, which approaches a consolidated cash statement, and in the form of Public Accounts. Each form differs somewhat from the other due to the different purposes served by these various forms of statistics. Federal expenditures in the first two forms have already been illustrated.⁹

The Public Accounts

Federal government expenditures are grouped into two categories in the government or public accounts, namely, budgetary and non-budgetary expenditures. Budgetary expenditures are primarily

⁹The data contained in these two forms are based chiefly on information contained in the Public Accounts of Canada. For information concerning a reconciliation between net general expenditure of the federal government as shown in Table II - III and the Public Accounts, see Dominion Bureau of Statistics, Financial Statistics of the Government of Canada, 1961, p. 17. For a reconciliation between the Public Accounts and government expenditures on a National Accounts basis, see Appendix A. For information regarding the expenditures deducted from the net expenditure of the federal government as shown in Table II - III to present this expenditure on the basis of the National Accounts, see Appendix C, Table C - II.

operating expenditures of government departments requiring annual Parliamentary appropriation, or which are authorized by statute, and which appear in the annual document of expenditure estimates tabled in Parliament. Beyond the scope of this document are various outlays such as loans, investments, and advances which are not considered as budgetary expenditures as the principal is usually repaid and in most cases they earn interest or produce revenue for the government. They form an important element in the financial operations of the government, and while they are not represented in the budget balance they usually have a significant effect on the government's cash position.

Budgetary Expenditures

Table II - IV sets out budgetary expenditures on a functional basis for selected years. Including expenditures from the Old Age Security Fund, which are usually shown in the budget,¹⁰ total budgetary expenditures have increased from \$4,787 million in the 1955 - 56 fiscal year to \$7,681 million in the 1963 - 64 fiscal year, an increase of approximately 62 percent. In 1963 - 64 the functions of defence, health and social welfare, the public debt, transportation and communications, and resources and industrial development absorbed over 80 percent of total federal expenditures. The table also indicates that since 1956 the pattern of expenditures on the various functions have changed. The relative importance of

¹⁰While the Old Age Security Fund is a non-budgetary account, the Minister of Finance considers it significant enough to warrant a presentation of expenditures including and excluding its effects.

TABLE II - IV

BUDGETARY EXPENDITURE CLASSIFIED BY FUNCTION

(\$ Million)

Function	Fiscal Year Ending March 31			
	1956		1964	
	Amount	%	Amount	%
Defence	1,769	39.9	1,723	25.1
Health, Welfare and Social Security	618	13.9	1,417	20.6
Public debt charges	514	11.6	994	14.5
Payments to provincial and municipal governments	359	8.1	290	4.2
Veterans Affairs	249	5.6	334	4.9
Transportation and Communication	341	7.7	786	11.4
Resources and industrial development	245	5.5	596	8.7
Education	10	.2	182	2.6
International Co-operation	33	.8	72	1.0
General government	291	6.6	466	6.8
Unclassified	<u>5</u>	<u>.1</u>	<u>13</u>	<u>.2</u>
Total Budgetary Expenditure	<u>4,434</u>	<u>100.0</u>	<u>6,873</u>	<u>100.0</u>
Old Age Security Fund Expenditure	353	7.0	808	11.0
Total	4,787		7,681	

SOURCE: Public Accounts of Canada, 1960 and 1964 (Ottawa: Queen's Printer). See Appendix C, Table C - III.

defence has declined considerably while health and welfare, public debt charges, transportation and communications, and resources and industrial development have increased in relative importance.

Non-Budgetary Transactions

Non-budgetary transactions are shown in the government accounts in two major categories. One category consists of transactions with respect to various trust funds, superannuation accounts, etc. The second major category consists of loans and advances to, and repayments by national, provincial and municipal governments, international organizations, and federal crown corporations. The disbursements of the crown corporations, however, are not included in either category. Certain other federal government activities relating to finance, such as direct loans made by federal organizations under established legislation and guarantees and insurance of loans made by approved financial institutions, are not included either.

The non-budgetary transactions as they appear in the public accounts are set out in Table II - V in summary form. In the 1964 - 65 fiscal year loans, investments, and advances amounted to \$726 million. The major portion of this sum was directed toward crown corporations. The table also indicates the effect that non-budgetary transactions have on the government's overall cash position. In 1964 - 65 the budgetary deficit was shown to be \$83 million, but non-budgetary transactions increased this deficit to \$428 million.

D. Scope For Fiscal Policy

In the total sphere of economic activity in Canada federal

TABLE II - V

BUDGETARY AND NON-BUDGETARY TRANSACTIONS

	Fiscal Year Ended March 31	
	1964	1965 (estimated)
<hr/>		
<u>Budgetary Transactions</u>		
Revenue	6,253	7,136
Expenditure	<u>-6,872</u>	<u>-7,219</u>
Deficit	-619	-83
 <u>Non-Budgetary Receipts and Credits (Net)</u>		
Repayments of loans, investments and advances	113	115
Annuities, insurance and pension accounts	384	553
Other receipts and credits	<u>165</u>	<u>188</u>
Total Receipts and Credits	662	856
 <u>Non-Budgetary Disbursements and Charges (Net)</u>		
Loans, investments, and advances	90	726
Other disbursements and charges	<u>235</u>	<u>474</u>
Total disbursements and charges	325	1,200
 Overall cash requirement (-) to be financed by increase in unmatured debt or decrease in cash balances		
	-283	-428
<hr/>		

SOURCE: House of Commons, Budget Papers, 1965 - 66. For a more detailed illustration of non-budgetary transactions, see Appendix C, Table C - IV.

expenditures, calculated on a national accounts basis and including transfers to other levels of government, presently comprise approximately 17 percent of the Gross National Product. But while total federal expenditure is relatively significant in relation to the level of Gross National Product, given the present composition and trends in government expenditure, the question is whether there is much scope for planning and making deliberate adjustments in federal expenditures for the achievement of fiscal goals. The primary functions for which the federal government is responsible may not be of the nature that expenditures in these areas are readily variable for stabilization purposes, nor may they be very significant for contributing to economic development and growth.

If expenditure programs are to be effectively employed in countering economic fluctuations which result in unemployment or inflationary tendencies, they must have certain qualities. Among these qualities are speed and flexibility in implementation. Furthermore, for purposes of combatting unemployment, expenditure programs should have considerable employment content or be capable of generating employment indirectly. They should also be of such a nature that a change in the scale of their operations will not have undesirably severe consequences in regard to other objectives of government policy such as the satisfaction of public wants and the distribution of income. On the other hand, for purposes of economic growth the requirements are that programs be both capacity-creating and income-generating. Economic growth, the increase in real national product, requires a growing demand for goods and services produced in the economy and expansion in productive capacity or capital formation.

The former without the latter will eventually lead to inflation while the latter without the former results in idle capacity and unemployment.

It would appear that among government expenditures those that meet these requirements most readily are direct resource-using expenditures of a capital nature. Maintenance, construction, and development in the fields of transportation, public works, and urban development, and natural resource and primary industry development are examples. Programs which are essentially subsidies or contributions to other levels of government or to business and which are directed to capital and development projects are others.¹¹ It is generally agreed that various expenditures of this nature which result in capital formation can be of considerable significance from the point of view of their program effects, that is, in contributing to economic growth and development.

There has, however, been much controversy over the effectiveness of capital projects as weapons of counter-cyclical policy. It has been argued that most capital projects do not meet the condition of speed in implementation as they take time to start and are also difficult to curtail once they are started.¹² An

¹¹With regard to the factor of employment generated by various government expenditures of a capital nature, see A. M. Strout, "Primary Employment Effects of Alternative Spending Programs", The Review of Economics and Statistics, XL (November, 1958), pp. 319 - 328.

¹²The literature is voluminous. See, for example, Julius Margolis, "Public Works and Economic Stability," Journal of Political Economy, LVII (August, 1949), pp. 293 - 303; S. J. Maisel, "Timing and Flexibility of a Public Works Program", Review of Economics and Statistics, XXXI (May, 1949), pp. 147 - 152; E. Jay Howenstine, "The

analysis of past performance may indeed indicate that expenditures on such projects may not have been effectively altered when conditions warranted. The effectiveness with which capital projects may be employed for counter-cyclical policy depends to a large degree on the nature and size of the project, the state of preparedness on the part of the government to begin the project, the urgency of the project, and administrative procedures for varying the rate at which it is undertaken. Considerable savings in time are possible if sufficient work in advanced planning is undertaken. Major engineering programs may be difficult to implement quickly or to terminate once they are begun, but other programs such as road construction and maintenance, work on conservation and resource development, river and harbour facilities, etc. may be accomplished piecemeal. Provided that sufficient time and effort are put into their planning, there is no reason to believe that programs in the fields of transportation, resource and industrial development, urban development, etc. could not be effectively utilized for both economic growth and stabilization purposes.

There is also the question of expenditures for the development of human resources which includes expenditures on health services,

Alleged Inflexibility of Compensatory Public Works Policy", Journal of Political Economy, LIX (June, 1951), pp. 233 - 241; and S. H. Slichter, "The Economics of Public Works", Readings in Fiscal Policy, ed. A. Smithies and J. K. Butters (Illinois: R. D. Irwin, Inc., 1955), pp. 38 - 50. For a general review of this entire area, see United States, Congress, Senate, Joint Economic Committee, Federal Expenditure Policy for Economic Growth and Stability, 1957, (Washington: Government Printing Office, 1957).

social welfare, and education. More and more attention has been focussed recently on these areas from the point of view of their significance for economic development and growth. It is generally agreed that investment in what is termed "human capital" can contribute considerably to the growth and development of the economy.¹³ Programs of this nature are of limited use, however, as anti-cyclical measures. From the point of view of social considerations it would be undesirable to decrease expenditures such as Old Age Pension payments or to cut back on the construction of hospitals and schools planned to be undertaken in any one fiscal year. In periods of recession such programs could of course be implemented at a more rapid rate than that called for in the original expenditure plans. Following the recession expenditures could be implemented at the rate specified in a revised long-run program.

Federal expenditures on the various functions of government take the form of direct expenditures on goods and services, transfer payments to individuals and organizations, subsidies to business, and transfers to other levels of government. The fact that government expenditures on goods and services generally involve direct government use of resources may often cause attention

¹³There is a long list of writings on this subject. See, for example, G. S. Becker, Human Capital (New York: Columbia University Press, 1964); E. F. Denison, The Sources of Economic Growth in the United States (New York: Committee for Economic Development, 1962); H. G. Johnson, The Canadian Quandary (Toronto: McGraw-Hill, 1963), pp. 227 - 235; T. W. Schultz, "Investment in Human Capital", American Economic Review, LI (March, 1961), pp. 1 - 16; and the articles in the Journal of Political Economy, Supplement, LXX (October, 1962).

to be focussed on this area for fiscal policy purposes. Federal expenditures, however, offer scope for fiscal policy in the other areas as well. Expenditures of the nature of transfers and subsidies may have a significant impact on income and economic activity depending on the recipients, the behavior of the recipients, and the effects the transfers have on the behavior of the recipients. Certain transfers or subsidies may be made for purposes of private capital formation or for price stabilization. Other transfers result in increased private incomes and consequent increased expenditures on goods and services. The possibility and extent of varying the latter transfer payments, however, depends on their nature and the conditions in the economy.

Expenditures on Goods and Services and Transfer Payments

As illustrated in Table II - VI federal government expenditures on goods and services have declined during the period 1956 - 63 from 8.8 percent of Gross National Product to 6.8 percent whereas transfer payments have increased from 7.7 to 10.5 percent. As a percentage of total federal expenditures, expenditures on goods and services decreased from 53.3 percent to 39.4 percent. In terms of aggregate federal expenditures, transfer payments consequently exert greater influence on the economy than expenditures on goods and services. Over one-half of the expenditures on goods and services are for defence which does not hold much scope for fiscal policy.¹⁴

¹⁴ Defence expenditures are not usually susceptible to deliberate changes for fiscal policy purposes. To the extent that they are maintained or remain stable, however, they do exert a certain stabilizing force on aggregate expenditure in the economy. To the extent that defence contracts are awarded to domestic industry they tend to be a sustaining factor for certain industries.

TABLE II - VI

FEDERAL EXPENDITURE BY MAJOR ECONOMIC CATEGORY

AS PERCENTAGE OF TOTAL AND AS PERCENTAGE OF

GROSS NATIONAL PRODUCT

(National Accounts Basis)

Economic Category	1956		1963	
	% of Total	% of G.N.P.	% of Total	% of G.N.P.
Goods and Services	53.3	8.8	39.4	6.8
Defence	35.8	5.9	21.2	3.7
Other	17.5	2.9	18.2	3.1
Transfer Payments and Subsidies	37.1	6.1	44.9	7.8
Transfers to Other Levels of Government	9.6	1.6	15.7	2.7
Total Expenditure	100.0	16.5	100.0	17.3

SOURCE: Dominion Bureau of Statistics, National Accounts, Income and Expenditure, 1961 and 1963. See Appendix C, Table C - I.

It will be noted, however, that the decline in the relative size of expenditures on goods and services is a result of the decreasing size of defence expenditure. From 1956 to 1963 relative expenditure on goods and services for purposes other than defence have increased slightly.

It was pointed out earlier that expenditures in the areas of transportation and resource and industrial development offered scope for fiscal policy, particularly in respect to short-term maladjustments. Returning to Table II - IV it can be seen that budgetary expenditures in 1963 - 64 included \$786 million for transportation and communications and \$596 million for resource and industrial development for a total of \$1,382 million or 20 percent of government expenditures. Furthermore, there has been a sharp increase in expenditures on these two functions. Since 1956 federal expenditures have more than doubled in both areas. These are also functions in which the major portion of the expenditures are for goods and services.¹⁵ Furthermore, crown corporations are very active in these fields. Current expenditures of the corporations on transportation, communication and other utilities totaled \$1,167 million in 1961 - 62.¹⁶

Grants to Provinces

Grants to provinces for specific purposes, that is, conditional

¹⁵In the fiscal year 1961 - 62 expenditures in the fields of transportation and communications, natural resources and primary industry, and trade and industrial development amounted to \$849 million, of which 54 percent was for goods and services, 38 percent for transfer and subsidy payments to the private sector, and 8 percent for transfers to other levels of government. See Appendix C, Table C - II.

¹⁶See Appendix C, Table C - VII.

grants, have risen from \$83 million in 1955 to \$902 million in 1965.¹⁷ These grants are generally provided in areas where the financial resources of provincial governments are inadequate for the governments to maintain or provide desired social services which fall under their jurisdiction. While the provinces administer these grants, certain conditions are imposed on them by the federal government such as minimum standards of service, periodic inspections, and an audit of the expenditures to ensure that the grant is properly applied to the purpose for which it was made. They are essentially cost-sharing programs in which the federal government agrees to grant financial aid for a specific program or service provided that the provincial government spends an equivalent or specified amount for the program in question. On this basis, the federal government can provide incentives and can participate in services under provincial jurisdiction, and consequently has a certain degree of influence on provincial expenditure policies.

While the major portion of conditional grants have been in the areas of health and welfare and education, contributions in cost-sharing programs in other areas such as resource development, transportation, municipal works, and agriculture have been increasing rapidly and offer possibilities for counter-cyclical and growth policy. Recent developments in federal-provincial fiscal arrangements, however, may well limit the extent to which shared-cost programs are undertaken in the future. The introduction of the "opting out" or "contracting out" clause in which

¹⁷ For an illustration of the trends in federal grants to provinces, see Appendix C, Table C - V.

a province may "contract out"¹⁸ of a federal conditional grant program in favor of a higher rate of tax abatement may in all probability decrease the influence of the federal government on the direction of provincial expenditures.

Unconditional grants, as implied, are made with no restrictions or specifications attached and consequently offer little scope for fiscal policy on the part of the federal government. Their use for fiscal purposes depends on the recognition by provincial governments of the need for such action.

Loans and Guarantees

From the nature of the federal government's direct loan and guarantee program and the amounts expended, it would appear that the impact of the program on the economy may be quite significant. These loans and guarantees, as illustrated in Appendix C, Table C - VI, are primarily for capital construction, development, and improvements. In the 1963 - 64 fiscal year direct loans totalled over \$550 million and the amount of guaranteed loans was even greater. Only to the extent that the direct loans are financed by federal advances to the agencies administering them are these loans included in the public accounts as non-budgetary disbursements. The guarantee programs, on the other hand, involve little use of public funds and therefore are omitted almost completely in the annual budgetary accounts. They may, however,

¹⁸For an account of these developments and the conditions for "contracting out", see Canadian Tax Foundation, Report of the Proceedings of the Eighteenth Annual Tax Conference (Toronto, 1965), pp. 209 - 218.

have a considerable effect on economic activity and, in the words of G. F. Break, "to the extent that they do, a significant portion of the influence of the Federal Government on incomes, spending, and prices is hidden from view" ¹⁹ Such credit programs not only directly stimulate the industry toward which they are directed by inducing spending which otherwise might not have taken place, but also generate economic activity indirectly in other industries and sectors of the economy. A measure of the influence of these programs on the basis of total disbursements tends toward oversimplification. A more concentrated type of analysis is required concerning such programs. Break has emphasized that

. . . there is a need of further supplementary material — an expansion of . . . analysis to include gross private loans authorized and disbursed through the insurance and guaranty facilities, an economic classification of the main purposes for which the funds are to be used, and, in addition, a comprehensive, quantitative analysis of the effects which these money flows are likely to have on various parts of the economic system. It need hardly be stressed that fiscal policy should take these extra-budgetary programs into account. ²⁰

Some of the direct loan programs have been established primarily for promoting employment and industrial development. For example, one of the reasons for the establishment of the Municipal Development and Loan Fund was to combat regional unemployment. It provides loans to municipalities, through the provinces, for municipal projects. Projects involving large

¹⁹United States, Congress, Senate, Joint Economic Committee, Federal Expenditure Policy for Economic Growth and Stability, 1957, (Washington: Government Printing Office, 1957), p. 432.

²⁰Ibid.

numbers of workers are to receive priority. Another example is the loan program of the Export Credits Insurance Corporation. It is authorized to provide direct long-term loans for export sales of capital goods. Eligibility for such loans requires that the Canadian content is not less than 80 percent and that the transaction gives rise to significant employment and industrial benefits to Canada. The government's home financing and urban development program administered by the Central Mortgage and Housing Corporation was also intended to be counter-cyclical and to provide employment.²¹

In summary, there appears to be appreciable scope for fiscal policy in the area of federal expenditures. This pertains to both the budgetary and the extra-budgetary transactions. It is not maintained, however, that government expenditure policy is, or can be, the single remedy for the problems of cyclical fluctuations and economic growth. All means available to the government should be employed if fiscal policy is to be effective. Depending on the nature of the problem, government expenditures may be

²¹ For an analysis of the effect of housing construction on labour income and employment and for an account of the effectiveness of the Central Mortgage and Housing Corporation's program as a counter-cyclical device, see H. H. Binhammer, "The Fiscal Implications of a Housing Program", Canadian Journal of Economics and Political Science, XXIX (August, 1963), pp. 336 - 347. Binhammer has concluded that "Aside from generating a large portion of labour income, other factors recommend residential construction as an excellent tool for counter-cyclical policy. Residential construction can be started quickly and concentrated in areas where a stimulant to economic activity is required. Moreover, because the construction of houses can be completed quickly, investment can be easily tapered off if need be." (p. 343).

an important part of this so-called "mix" of various fiscal tools. Various federal expenditure programs can be very significant in contributing to economic growth. There is also a fairly significant area of expenditure which lends itself to policies to combat temporary economic fluctuations. In periods of extended recession federal expenditures in practically all fields may be utilized to promote economic recovery. There is also the fact that the total expenditure of all three levels of government, amounting to roughly 32 percent of Gross National Product in 1963 - 64, exert a strong stabilizing force on the economy in the event that other components of aggregate demand should be subject to severe fluctuation. Furthermore, assuming that co-operation and co-ordination in fiscal policy is attained, government expenditure policy could be a very influential weapon of fiscal policy indeed.

E. Attitude of The Canadian Government

To Fiscal Policy

Beginning of Fiscal Policy in Canada

Fiscal policy first came to prominence with the Great Depression of the 1930's. Prior to 1930 the old doctrine of annually balanced budgets was quite firmly entrenched in economic thinking, and in the early years of the depression continual efforts were made by the Canadian government to balance the budget by maintaining high tax rates to meet increasing government expenditures. From the period 1935 to 1939, however, under the influence of leading economists of the time, government fiscal thinking underwent a change and the government began to recognize more and more the significance of fiscal policy as a means of influencing economic

activity and achieving economic goals.²²

World War II erupted before solutions to the problems of the depression were reached. In the war economy problems of unemployment and idle productive facilities disappeared. But the concern with these problems did not vanish, for it was anticipated that with the termination of the war the difficulties of the depression would return, and added to them would be the dislocations brought about in the economy as a result of the war. Consequently, during the period of the war the government became increasingly concerned with the reconversion of the wartime economy to a peace time one following the termination of hostilities. There was also a problem of effecting reconversion without returning to the depressed conditions of the pre-war period. Various Cabinet and Parliamentary committees were established to consider these problems.²³ Realizing that it could not accomplish the work of reconstruction alone, however, the federal government undertook the task of obtaining provincial co-operation in regard to this matter.

²²For an account of the attitude of the government of Canada toward fiscal policy prior to 1940, see Irving Brecher, Monetary And Fiscal Thought And Policy In Canada, 1919 - 1937 (Toronto: University of Toronto Press, 1957).

²³See Canada, Advisory Committee On Reconstruction, Report, Sept. 24, 1943, and Canada, Advisory Committee On Reconstruction, Conservation And Development of Natural Resources, Final Report of the Subcommittee, Sept. 24, 1943. For an account of the other matters that were considered by the Advisory Committee in 1943, see its reports entitled Agricultural Policy, Publicly Financed Construction Projects, Housing and Community Planning, and Post-War Employment Opportunities.

In April 1944 the government introduced a bill for the creation of a Department of Reconstruction which was to be concerned with such matters as the re-employment of Canadians whose occupations had been channeled to war activities, the conversion of wartime industry to peacetime industry, the restoration of railroads, highways, and other capital equipment which had deteriorated during the war, the planning of public works and services, and the development of projects to provide alternative employment while wartime industries were being converted for peacetime purposes.²⁴ While the original Department of Reconstruction was to have a special responsibility for the planning of public projects and services, it was to be primarily concerned with co-ordinating the activities of other departments for the provision of employment opportunities. It later adopted various duties which had been the responsibility of other departments and its title was changed to the Department of Reconstruction and Supply.

The concern for high levels of employment and income was thus expressed very early in the war years by those who looked to the future and the aftermath of the war. In 1945 the earlier activities, discussions, and Committee deliberations were brought to a head. Government policy on income, employment, the price level, and standards of living were carefully enunciated in a

²⁴See Canada, House of Commons Debates, April 17, 1944 pp. 2084 - 2101.

White Paper entitled Employment and Income which was tabled in Parliament.²⁵ In the White Paper the government declared unequivocally its "adoption of a high and stable level of employment and income, and thereby higher standards of living, as a major aim of government policy".²⁶ The White Paper proposed the "deliberate use of public investment expenditure as a permanent instrument in employment policy".²⁷ The government did not believe that the expected post-war employment problem could be solved entirely by huge government capital expenditures, however, nor did it believe that it would be desirable to attempt to do so.

²⁵Canada, Department of Reconstruction, Employment And Income (Ottawa: Queen's Printer, 1945).

²⁶Ibid., p. 23.

²⁷Ibid., p. 16. This policy was to follow two lines, namely:

- "(1) the undertaking of advance planning of all necessary and desirable Dominion projects so that there may be available a 'shelf' of soundly planned projects, ready for execution when prospective employment conditions make it desirable to increase public investment expenditures. Since in the inter-war years the public investment expenditures of provincial and municipal governments have been much greater than those of the Dominion government, it will be an essential part of such a policy that advance planning on the part of these governments should be encouraged, and without interfering with provincial and municipal decisions in respect of the direction of their own expenditures, co-operation should be sought on the timing of such expenditures;
- (2) the implementation, in co-operation with the provinces, of a new Dominion policy of expenditures on the development and conservation of natural resources."

Much of the responsibility for implementing the public investment program belonged to the Department of Reconstruction. It established co-ordinators for public projects and for natural resource development, and it appointed local regional councils in the provinces to keep the Department informed of employment conditions in their respective areas and to recommend suitable public projects.

To achieve its stated aim the government proposed to attack the problem on other fronts as well. It proposed to stimulate export trade and private investment, to introduce measures to prevent declines in income which might become cumulative, to safeguard low family incomes,²⁸ to encourage research by private industry, and to assist in the placement and training of workers.

The government's preoccupation with, and elaborate preparations for, reconstruction and the achievement of "a high and stable level of employment and income", a much used phrase at that time, are evidence of the extreme importance that was attached to this problem during the latter part of the war and the immediate post-war period. Fiscal policy had never before, and has never since, been emphasized to such an extent by the federal government, nor have such elaborate and definite actions been planned to put it into practice.

The difficulties of the reconstruction period did not arise in the severity that was envisaged. Reconversion took place rapidly, and the demand for consumer and durable goods that had been repressed during the war period not only kept productive facilities operating at capacity but provided for rapid expansion.²⁹ The objectives that had

²⁸The government had earlier enacted statutes such as the Unemployment Insurance Act of 1940 and the Family Allowance Act of 1944 which, it was believed, would partly meet this problem. The government also indicated its willingness to institute contributory old age pension and health insurance schemes.

²⁹By March, 1946, of those plants that faced a reconversion problem following the termination of the war, over half had completed the reconversion process. Of the remainder, 75 percent completed the process before the end of the year. Approximately 45 percent of the plants had completed or were undertaking modernization or expansion programs, and a large number of new establishments were coming into

been declared to be of primary importance were achieved largely through the market mechanism. The Department of Reconstruction did undertake the task of planning and co-ordinating public projects in the immediate post-war years but not nearly to the extent that had been anticipated.³⁰ By 1949 it was no longer considered necessary to have a separate department for this purpose, with the result that its functions were redistributed and the department went out of existence.³¹

But if anyone harboured the illusion during these early years that economic instability was a thing of the past and that the market mechanism alone was capable of achieving and sustaining the objectives that had been declared in 1945, this was to be shattered in subsequent years. By 1950 the buoyant economy started to sputter and the unemployment problem began to reappear. The elaborate plans enunciated in 1945 for coping with such a problem, however, appeared to have been neglected in the meantime. The "shelf" that was to have been filled with well-

operation to produce for the peace-time market. Of the 1,000,000 people who gave up their wartime occupations in the fall of 1945, close to 800,000 had found employment by March, 1946. For C. D. Howe's statement on this, see Debates, March 20, 1946, pp. 112 - 120.

³⁰In fact, the government was forced to prune its public works and other construction programs in order to avoid bidding against private enterprise for resources and thus adding to inflationary pressures. In 1946, of the \$10 million voted for reconstruction projects to take care of spotty unemployment only \$500,000 was actually spent. Of the \$5 million voted in 1947 only \$591,000 was spent. By June 1947, the staff of the Department of Reconstruction had decreased from 5,000 to 600 in number. See Debates, July 15, 1947, p. 5718.

³¹See Debates, November 26, 1949, pp. 2284 - 2297.

planned and ready-to-execute projects for meeting unemployment situations was bare.³² There also appeared to be a change in government attitude. In his budget speech of 1950 the Minister of Finance, D. C. Abbott, stated that, even though unemployment had increased by 1 percent of the labour force since 1949, much of the unemployment was regional and, in his words, "the central government cannot and should not attempt to assume responsibility for these regional problems."³³

Government thoughts and plans of 1945 were conceived in an atmosphere of fear of serious post-war unemployment. When this did not materialize the importance attached to policies designed to maintain "high levels of employment and income" appeared to dwindle. Plans of fiscal policy to meet any future situation of instability in the economy, especially downward trends, were not prepared, and the subsequent years witnessed the introduction of such policy on an ad hoc basis to meet these situations after they had presented themselves and were fairly well advanced. The following outline will serve to give some indication of the Federal government attitude toward fiscal policy in the post-war period and the extent to which emphasis was placed on government expenditures in the policies pursued.³⁴

³²As one member of Parliament remarked:
 "... this program, as set forth in the white paper, has not been fulfilled. We come into an unemployment situation in which the government admits that it has no shelf of public projects planned over a period of years, as there should have been, to which effect could be given when unemployment arose." Debates, March 1, 1950, p. 367.

³³Debates, March 28, 1949, p. 1210.

³⁴For one account of federal fiscal policy in the period 1946 - 56 and its effectiveness in terms of contributions to aggregate demand,

Fiscal Policy, 1945 - 1965

The 1945 White Paper clearly proposed the use of the budget for purposes of fiscal policy and indicated the government's acceptance of surpluses and deficits as a result:

The government will be prepared, in periods, when unemployment threatens, to incur the deficits and increases in the national debt resulting from this employment and income policy, whether that policy in the circumstances is best applied through increased expenditures or reduced taxation. In periods of buoyant employment and income, budget plans will call for surpluses. The Government's policy will be to keep the national debt within manageable proportions, and maintain a proper balance in its budget over a period longer than a single year.³⁵

In the post-war period the Canadian economy has experienced periods of fairly rapid expansion and high levels of employment as well as periods of sluggishness and relatively high rates of unemployment.³⁶ The government has generally adhered to the policy of counter-cyclical budgeting in this period, as was declared in 1945, incurring large budgetary

see J. Harvey Perry, "Some Aspects of Recent Fiscal Policy", Canadian Tax Journal (Toronto, 1957), pp. 285 - 298. Perry submits that by the mid 1950's there was a "gradual decline in the conscious use of fiscal policy and a much greater dependence on monetary techniques. . . ." (p. 298). Fiscal policy, he states, had not been rejected but "rather it would appear that its possibilities and limitations have been more clearly delineated in the light of the experience of the post-war years" (p. 288). This may be true of fiscal policy concerning inflation. It must be remembered, however, that the primary concern with fiscal policy had from the beginning been its use for the stimulation of a depressed economy, and up to the mid 1950's the opportunity to test the possibilities of government revenues and expenditures for this purpose had never really presented itself to any serious extent. The recession beginning in 1957 saw a revival of interest in fiscal policy and considerable emphasis was to be placed on it in the following years.

³⁵Income and Employment, p. 21.

³⁶For a brief review of Canada's post-war economic performance in terms of economic growth, employment, etc., see Economic Council of Canada, First Annual Review, Economic Goals for Canada to 1970 (Ottawa: Queen's Printer, 1964), pp. 7 - 30. See also, F. T. Denton and Sylvia Ostry, An Analysis of Post-War Unemployment, Staff Study No. 3 prepared for the Economic Council of Canada (Ottawa: Queen's Printer, 1965).

surpluses during the early years of rapid economic expansion in which inflationary pressures prevailed and budgeting for large deficits in the recession period following 1957. Furthermore, this policy was to be rather emphatically restated on various occasions by Ministers of Finance in their budget speeches during this period.

During the years from 1945 - 49 the government's concern was primarily with inflation. The general policy that was followed included the gradual removal of wartime controls and retrenchment in government expenditures. The policy also included reductions in taxes from their high wartime level. While tax reductions during a period of inflation would appear to be contrary to accepted fiscal policy, it must be remembered that taxes during the war were exceedingly high by previous standards and there was considerable public pressure to have them reduced following the war. The government's policy was to reduce taxes gradually where they were impeding work and production and in this way provide a stimulant to production to satisfy excessive demand, but otherwise to keep taxes as high as reasonably practical to produce a surplus and pay off the debt. During this period overall employment was high, although there was considerable criticism in the House of Commons to the effect that the government did not introduce special measures to alleviate the unemployment problem in certain regions such as the Maritimes.

From 1950 - 1956 the economy enjoyed a high degree of prosperity with the exception of a brief slump in 1954. The post-war inflationary tendencies were still present in the economy during this period and the general policy followed consisted of restrictions on credit, the urging of greater saving and less consumption, deferred depreciation allowances,

and the pursuit of economy and retrenchment in government expenditures. The anti-inflationary policies regarding investment pursued during 1951 and 1952 were directed to allow the government to carry out its defence program without contributing to cost-push inflation.³⁷ By discouraging private investment and holding down government capital expenditures on non-urgent projects, resources would be made available for the defence program. Government expenditures for defence, however, are themselves inflationary in the sense that military equipment is not adaptable to personal use and the income received by persons as a result of defence production is not matched by production for consumers' use.

Fiscal policy in the early 1950's appears to have been concentrated on retrenchment in government expenditures to avoid competition for employed resources and in the 1955 - 56 fiscal year, as a continuation of the policy of retrenchment, the main budgetary estimates were reduced from their 1954 level. Taxation was not considered as a very effective counter-cyclical weapon and the attitude of the government in this respect was voiced by D. C. Abbott, the Minister of Finance, when he stated:

. . . taxes are a clumsy instrument . . . uncertain of their effects, and in my experience misunderstood when applied for special economic reasons, as distinct from the direct raising of revenue.³⁸

The 1957 - 62 period was one of economic adjustment coupled with

³⁷Debates, April 8, 1952, p. 1244.

³⁸D. Abbott, "Savings, Investment, and Inflation: A Canadian View", Savings In The Modern Economy, eds. W. Heller, F. Boddy, and C. Nelson (Minneapolis: University of Minnesota Press, 1953), p. 32.

inflationary tendencies. Government policy was directed at curbing the economic decline that had set in and at promoting economic recovery. In the beginning of this period, because of a backlog in social capital projects, the government was inclined to view government expenditures as more appropriate and effective in promoting economic recovery than tax reductions. To this effect the Minister of Finance, D. M. Fleming, commented:

The advocates of tax reduction argue that by leaving more money in the hands of individuals, consumer spending will be stimulated and more savings will be available for productive capital investment. But I believe that experience has shown that while this may happen to some extent, unless other stimulating measures are taken much of the tax savings to many taxpayers tends to be idle. It is neither wholly spent nor put into productive investment. A program of public investment has the obvious advantage of providing employment for idle or underemployed manpower and equipment.³⁹

The policies from 1958 to 1960 included large expenditures for national development and social security, housing loans, increased federal transfers to provinces, investment in community facilities, small business loans, aids to technical education and training, etc. while introducing few significant changes in taxation.⁴⁰ In 1958 the government claimed that public investment had been increased by 17 percent from the 1957 level and had "offset almost two-thirds the decline in business investment."⁴¹ The government also claimed that

³⁹Debates, June 17, 1958, p. 1242. For a brief account concerning the emphasis placed on expenditure policy at the beginning of the 1957 recession, see K. W. Taylor, "Fiscal Policy", The Canadian Economy Selected Readings, ed. J. J. Deutsch et. al (Toronto: MacMillan Co. 1962).

⁴⁰In December 1957 the rate on the first \$1,000 of taxable income was reduced from 13 percent to 11 percent and the rate on the second \$1,000 was reduced from 15 percent to 14 percent. In the fiscal year 1959 - 60, in an attempt to combat inflationary tendencies, the tax rate on taxable income over \$3,000 was increased by one percentage point for 1959 and by an additional percentage point for 1960. Also, corporation taxable income in excess of \$25,000 was to be taxed at 47 percent rather than at the previous rate of 45 percent.

⁴¹Debates, April 9, 1959, p. 2406.

the government action of making funds available for housing had resulted in a 25 percent increase in residential housing construction in 1958.

Toward the end of this period the government began placing ever increasing emphasis on economic growth and began to stress incentives to private industry through tax policies. In 1960 to 1961 the Minister of Finance, rather than relying primarily on expenditure policies, attempted to influence private investment, production, and scientific research and technological development by concentrating on tax changes and tax incentives.⁴²

The year 1962 marked the beginning of an economic recovery. To stimulate this upswing the government continued to budget for large deficits and placed emphasis on the unemployment problem. It was recognized that a considerable amount of unemployment was of a regional and seasonal nature. Consequently, the measures introduced to alleviate unemployment were directed toward specific groups and areas rather than toward increasing the overall employment rate through a general increase in aggregate demand. Emphasizing the disparities in the unemployment rates between the various geographical regions of the country, the Minister of Finance, in his budget speech for the fiscal year 1964 - 65 stated:

The wide diversity of these figures . . . suggests that broad,

⁴² In 1960 tax revisions were proposed calling for the 21 percent corporation income tax to be applied to corporate incomes below \$35,000 rather than the existing level of \$25,000, and the repeal of the 4 percent surtax on investment income to encourage investment. In 1960 the 7½ percent excise tax on automobiles was repealed in an attempt to stimulate the depressed automotive industry in Canada. As an incentive to research it was also proposed that businessmen could deduct all expenditures of a capital nature made in respect to scientific research.

general attacks on employment will be less useful than they have been in the past. Accordingly our plans and policies are increasingly designed to meet the special needs of areas of the country or groups of the population confronted with special difficulties and problems.⁴³

Among the specific measures introduced in 1963 and 1964 in the government's tax and expenditure program designed to promote regional industrial development and to combat regional and seasonal unemployment were the following: accelerated depreciation and a three-year tax holiday for new manufacturing and processing businesses in designated areas, an increase in the rate of capital cost allowance from 30% to 50% on certain equipment used by the construction industry, the continuation of and increased payments under the Municipal Winter Works Incentive Program, the winter housing bonus program, the Municipal Development and Loan act, the Older Worker Employment and Training Incentive Plan, and the Manpower Consultative Service under which the government contributes to unemployment research and pays one-half of the cost of shifting displaced workers to communities where work is available. These policies were continued into the 1965 - 66 fiscal year. In his budget speech in April, 1965, the Minister of Finance announced a 10 percent reduction in personal income taxes up to a maximum of \$600. The primary reason given for the tax cut in this "growth budget" was to increase public purchasing power and in this indirect way to stimulate economic growth.

In general, the use of government expenditure as a device for stabilization and the promotion of economic growth in the postwar period

⁴³Debates, April 10, 1962, p. 2692.

appears to have been given as much, if not more, attention as tax policies for the same purposes. The fear of a depression following the war led to elaborate plans and preparations to maintain economic activity at a high level. Considerable emphasis was placed on government expenditure policies for this purpose with the establishment of the Department of Reconstruction. The period 1945 to 1957 experienced a relatively high rate of growth coupled with inflation which led to the retrenchment of government expenditures. The recession and the high rates of unemployment which lasted generally from 1957 to 1962 saw increasing emphasis placed on fiscal policy as an instrument to promote economic recovery. Once again, as in 1945, considerable emphasis was placed on expenditure policies by maintaining high and increasing levels of expenditure in general areas and introducing various specific expenditure programs, while holding taxes relatively stable except for slight increases in tax rates on higher incomes and on luxury goods to combat inflationary tendencies. Following 1960 more liberal use began to be made of specific tax measures for economic stability and growth purposes. With recovery on the way in 1962 the government began to concentrate on promoting economic development, and alleviating unemployment, in depressed localities with specific expenditure and tax incentive programs.

III

THE CANADIAN BUDGETARY PROCESS

The presentation of the annual government budget document is the highlight of a budgeting process which continues throughout the fiscal year. It is through this process that expenditures are determined, examined, and authorized, and consequently through which fiscal policy decisions are made.

To determine the effects of expenditure proposals introduced as fiscal policy and to determine the contribution made to the achievement of fiscal goals by expenditures introduced primarily for other purposes requires an analysis of the impact of expenditures on the economy. To what extent is such an analysis, in the form of spending and program effects, undertaken in the present budgetary process? The datum or information on which the analysis and evaluation of government expenditures is based is related to, and stems largely from, the form in which expenditures are classified. Are the present expenditure accounts and related data conducive to an analysis of the spending and program effects of expenditure proposals? What are some of the other problems which impose limitations on the active utilization of fiscal policy?

A. Organization And Procedure

With respect to the expenditure side of the budget two of the most significant organizations or agencies of government involved in the

budgeting process are the Treasury Board and the Department of Finance.

The Treasury Board is a committee of the Queen's Privy Council of Canada and is composed of six members of the Council. The members who comprise the Treasury Board, however, are always Cabinet ministers. Until very recently the Treasury Board was presided over by the Minister of Finance, but it is now presided over by the President of the Privy Council who is named to be President of the Treasury Board. The Board is served by a secretariat directed by an officer designated as the Secretary of the Treasury Board.

The Treasury Board is the expenditure control agency of the government. It is responsible for determining and co-ordinating the financial measures or programs that are to be presented before the Cabinet for consideration and approval. Through its function of establishing priorities among the many competing expenditure programs of the various government departments, the Treasury Board in government can be said to act in lieu of the price mechanism in the market economy in the allocation of resources.¹

The Department of Finance is primarily concerned with the preparation of the revenue side of the budget, with taxation and tariff policies, audit services, the accounts of the government, analysis of various expenditure programs, and with forecasting and analyzing conditions and trends in the economy and in surveying the budget in the

¹For a more detailed description of the organization and functions of the Treasury Board, and of the organization and procedure of the Canadian budget system in general, see Appendix D.

context of the economy as a whole. The office within the Department of Finance which is responsible for controlling the actual disbursement or release of funds is the Comptroller of the Treasury. The Comptroller's office is also responsible for the maintenance of government revenue and expenditure accounts.

The Financial Affairs and Economic Analysis Division of the Department of Finance is responsible for forecasting economic developments, analyzing the requirements of the economy, and locating bottlenecks and imbalances. This Division is responsible for preparing the Budget White Papers which accompany the budget speech. Within the Department of Finance there is also a Resources and Development Division which has the function of conducting an analysis of new departmental projects in the fields of natural resources, industry, atomic energy, etc. This analysis is undertaken in close liaison with the departments concerned at the stage prior to the submission of the proposal of the project to the Cabinet for approval in principle, following which it becomes departmental policy.

The budgeting procedure in regard to government expenditures follows a prescribed routine. Shortly following the beginning of each fiscal year the various government departments and agencies are required to submit estimates to the Treasury Board secretariat of their expenditure requirements for the following fiscal year. The Treasury Board indicates the commencement of the estimates process by means of a formal letter of instruction to all departments. This letter is accompanied by an outline of general financial policy for the coming year in the light of economic conditions as determined by the Minister of Finance.

and his staff, and departments are requested to take this policy into consideration when determining their expenditure plans and programs.

The departmental expenditure estimates are prepared under the direction of the deputy minister, and after being reviewed and approved by the Minister of the department concerned they are forwarded to the Treasury Board secretariat. The secretariat conducts an examination of the estimates generally from two points of view: cost and policy. With regard to cost the secretariat must be satisfied that all expenditure items are reasonable for the proposed program. The policy review is conducted to ensure that all new programs have received Cabinet or Treasury Board approval in principle prior to their inclusion in the estimates. Generally, certain expenditure reductions are effected during this review process following which the secretariat transmits the revised estimates to the President of the Treasury Board. The Board meets daily for approximately three weeks in late November and early December to review and discuss the estimates. The Board may reject any expenditure proposal that it decides is not in line with the broadly stated budget objectives and may postpone or cancel proposals of lesser priority. Finally the estimates are submitted to the Cabinet for final review before being presented to Parliament for authorization. The estimates are generally tabled in Parliament sometime in February.

The form in which the expenditure estimates are prepared by departments for submission to Treasury Board is basically the same form in which they are tabled in Parliament in the document called Estimates and is a prescribed one.² Expenditures are classified on the basis of

²A detailed account of the present form of the expenditure estimates is presented in Appendix D, pp. 199 - 216.

established objects or items of expenditure, such as salaries, travel, materials, and supplies, repairs and upkeep, etc. for each major departmental operation or activity. These items are referred to in the expenditure classification scheme as the "standard objects of expenditure". Furthermore, in the present classification scheme various operations in a department are combined into principal groups of expenditure, each of which has been assigned a permanent vote or appropriation number. It is on the basis of these groupings that Parliament considers the estimates and makes appropriations for departmental operations.

In addition to those expenditures for which Parliament makes annual appropriations, there are also other expenditures which appear in the budgetary estimates for which such appropriation is not required. These are expenditures authorized by statute or what are known as statutory appropriations, which Parliament has agreed should not be subject to annual review and appropriation. All non-budgetary items, however, except expenditures from the Old Age Security Fund, are not included in the estimates document presented to Parliament.

The House of Commons considers the estimates as the Committee of Supply, which is a committee of the whole. The Minister of each department is responsible for steering the estimates of his department through the Committee and is expected to be present to answer any queries regarding departmental policy or any of the individual expenditure items. The expenditures of various departments may also be submitted to smaller Parliamentary committees, such as the Standing Committee on Estimates, for more thorough examination. Following the appropriation, disbursement, and expenditure of funds Parliament conducts a final examination of government

financial transactions through the Standing Committee on Public Accounts. This committee is responsible for examining the manner in which approved budgetary plans are administered by reviewing the Public Accounts, as prepared by the Comptroller of the Treasury, and the Report of the Auditor General. The Auditor General is an officer of Parliament who is responsible for conducting a post-audit of departmental expenditures and reporting the results of his findings to Parliament.

One other important feature of the budgetary procedure is the Finance Minister's annual budget speech before the House of Commons shortly following the commencement of the new fiscal year. In the speech expenditures and revenues are brought together and proposals of changes in the tax structure and tax rates are introduced. The budget speech is accompanied and supplemented by the Budget White Papers which trace developments in the economy in the previous fiscal year and set out the highlights of government financial operations during that year.

B. Limitations of the Budgetary System Regarding

Expenditure Analysis and Fiscal Policy

Implementation

In determining and planning individual expenditure proposals to be included in their estimates, and which may be generally classed in the category of expenditures for purposes of resource allocation, government departments in most cases do not conduct an analysis of the impact of the expenditures on employment, production, and economic growth. Nor do the expenditure accounts, the type of evaluation conducted by the Treasury Board in respect to resource allocation during the annual estimates review process, or the analysis by other agencies

within the Department of Finance shed much light on the probable effects of such expenditures from the point of view of fiscal objectives.

Expenditure Evaluation and Resource Allocation

Expenditure Accounts

The present form in which expenditure proposals are prepared does not facilitate effective planning or objective evaluation. The classification of expenditures on the basis of organizational units and objects of expenditure does provide information concerning the question of where public funds are going and, in general, what each unit intends to purchase. In this manner areas of responsibility are established and accountability is served. But objects of expenditure do not indicate the purpose of expenditures in terms of ends or objectives to be achieved or the benefits which are expected to accrue.

Planning of Expenditures

Planning consists of the establishment of a course of current and future action. It is a process of stating in definite terms when an expenditure program is to be undertaken, how long it will take to complete, how much it will cost, why it is in the public interest, whether it involves commitments for continuing expenditures and the like. It is essential to budgeting from the point of view of resource allocation, income distribution, and fiscal policy.

In the federal government very little has been done in the past in the way of preparing long-term expenditure plans, and it has only been in recent years that departments have been required to submit three-year forecasts of expenditures along with their annual submissions.

Prior to the introduction of this system of forecasting, the preparation of estimates and their appraisal by Treasury Board was on a year-to-year basis. At present forecasts are made on the basis of the vote structure of the Estimates, and consequently they are not formal plans in terms of what is expected to be accomplished. Only for construction projects can the present form of forecasting be considered planning in the sense that an indication is given as to what is going to be constructed and when, how much it will cost, and how much will be spent on the project in each fiscal year.

The reliance on past trends in expenditures on standard objects for determining current year estimates or for projecting figures for operating expenditures cannot be considered as planning. There is evidence that departments rely on this method considerably and do not appear concerned with actual intended purchases of resources and materials within each individual object to arrive at the lump sum figure it represents. Considerably more could be achieved in strengthening the planning process in departments. Most departments do not have a formal planning function and do not prepare formal planning documents which could form the basis of the estimates process.

Treasury Board Review

One of the major problems confronting the Treasury Board and its staff in the expenditure evaluation process is the absence of a market test of efficiency by which departmental programs may be appraised. As was mentioned previously, the function of the Treasury Board in government is to act in lieu of the price mechanism in the market economy. Treasury Board analysts therefore require some objective

criteria as a basis on which expenditure proposals may be examined and evaluated with a view to establishing priorities among the proposed programs. Without such criteria the estimates review process would consist of a single exercise in judgment and a conflict of opinion where differences between Treasury Board Officers and departmental officials arise.

The reference to objective criteria for evaluating expenditure programs relating to resource allocation implies that factors relevant to the appraisal of programs be measured if it is feasible to do so. It does not suggest that the criteria be purely objective, for it is impossible to develop such criteria. Among the wide range of effects of a program which may be pursued in an evaluation of the program are usually certain effects which are not susceptible to objective valuation or measurement.³ This necessitates judgments regarding the values to be placed on these effects. If cost-benefit analysis is attempted it therefore must be realized that certain benefits can only be estimated on the

³On the matter of measuring benefits Jesse Burkhead has divided measurement problems into three broad classes: "The first are the cases where not even primary gains can be measured with precision, let alone indirect and intangible gains. The second class embraces cases where primary gains can be measured with some accuracy, but where secondary and intangible gains, not susceptible to measurement, may be more significant than the measurable gains. The third class consists of the cases where nonprimary gains do not predominate and where some rather precise measurements of gains and costs are possible" In the first class Burkhead includes national defence and public education. In the second class he includes programs such as urban renewal. In an urban renewal program, which includes slum clearance, street and housing construction, the provision of public parks, etc., certain benefits such as increases in property values and in economic activity may be measured in dollar terms. But it is difficult to measure such intangible benefits as the reduction in crime and disease rates and the improvement in the appearance of the community. The third class includes irrigation and land reclamation projects and similar projects in the area of resource development. See

basis of subjective judgments.⁴ The extent to which subjective valuation will be necessary will depend on the nature of the program and the benefits taken into consideration in computing the cost-benefit ratio.

Few of the departmental submissions of estimates contain a detailed quantitative justification of the expenditure proposals. In most cases where a department provides a continuing service, little or no formal indication is given as to whether the service is actually a continuing necessity. Seldom is information contained in the formal submissions regarding the expected benefits of the service or project as opposed to the costs. Attention appears to be concentrated on the standard objects or items and on changes in the amounts expended for each object.

It is difficult to develop and apply criteria, such as cost-benefit ratios, to expenditure proposals in the form they are presently prepared and submitted to determine the value of an expenditure program and to establish priorities. What useful criteria for establishing priorities can be applied to proposals when they are presented in the form of telephones, stationery, repairs and upkeep, or in the form of

Public Finances: Needs, Sources, and Utilization, Report of the National Bureau of Economic Research (Princeton: Princeton University Press, 1961), pp. 352 - 364.

⁴One of the benefits of highway improvement is a reduction in the number of accidents and consequent loss of human life. But the value of human life is a subjective matter. A judgment must be made regarding the value to be placed on human life if this factor is to be considered in the appraisal of a highway project. For a discussion of problems of this nature, see D. M. Winch, The Economics of Highway Planning (Toronto: University of Toronto Press, 1962), pp. 71 - 92.

the other standard objects? Nor can criteria be readily applied to vote descriptions and their subdivisions where objectives or end products are not specified.

While the Treasury Board has advanced toward objective appraisals of certain expenditure programs, the process is on a very unsystematic and ad hoc basis and is far from adequate. The Board, in its expenditure review, still relies basically upon concepts such as trends in expenditure by standard objects which, by including changes in the price level, does not appear to be an effective tool for program analysis. The starting point in the preparation and review of expenditure estimates are the estimates of previous years. Future expenditure requirements are built on the records of past years and there is a tendency to accept established services and programs without a re-examination of their purposes and the direction in which they are going. Basically there is little consideration given to the question of whether a particular program continues to be justified for the year or years ahead. The attitude appears to be that the existence of the programs in the past is sufficient justification for their continuation in the future, and that the only aspects that merit attention are the proposed increments to them.⁵

In summary, the present analysis of expenditures by Treasury Board is inadequate. Objectives and accomplishments are not readily determinable, expenditure estimates are not geared to plans and little use is made of objective criteria for establishing priorities. Treasury Board officers rely primarily on their experience when they are making

⁵
See Appendix D, p. 220..

judgments regarding proposed expenditure programs.

Impact of Expenditures on the Economy: The Analysis of Program and Spending Effects

Under the present system it is very difficult to evaluate the probable impact of the government's budget on the economy. Nor does the system permit an estimate to be made with any degree of confidence of the economic consequences of any specific expenditure or change in expenditure. This is not presented in the budget speech and it is doubtful that the Minister of Finance clearly understands how his budget is likely to affect the economy. It is quite apparent that the Treasury Board is generally not concerned with analyzing the effects of expenditures on the economy in its annual estimates review. This also applies to the House of Commons during its review. Other than generalizing about economic conditions and broad government policy little attention is given in Parliament or its committees to the government's contribution to employment, income, and production in quantitative terms. In fact there is no quantitative framework provided in which government proposals can be examined in this respect at any level. The expenditure classification scheme and basic budget concepts which are used have been developed primarily for purposes of budget control and not for purposes of economic information.

Economic Conditions and Expenditure Determination

In the process of determining priorities among expenditure programs it appears that government departments give weight to economic conditions or such factors as employment only when instructed by the government. Otherwise, economic conditions and the probable

impact of expenditure programs on the economy from the point of view of fiscal goals generally receive little or no attention. This also applies to Treasury Board.

The Department of Northern Affairs and National Resources normally devotes little attention to the economic impact in terms of employment in determining its annual expenditure program. Projects must justify themselves on social and other economic grounds. For instance, a flood control project is evaluated on the basis of its value in preventing floods and losses resulting therefrom. Nevertheless, there have occurred instances when certain care has been taken to ensure that most of the workers employed for the construction of a project came from the surrounding area if it is an area of relatively high unemployment. In a period of major recession the department would generally be subjected to considerable pressure to introduce projects for their employment effect. In such cases projects which are highly desirable from the point of view of resource allocation are not cancelled or postponed in favor of other projects which may have greater employment content or which are related to areas of high unemployment. Additional projects would be introduced in which priority is given to depressed areas and the unemployment problem.

To take another example, the Department of Transport does not give any consideration to the fact that one area may be depressed and that its projects may alleviate unemployment or increase the income of the people of the area. Such factors are not taken into account in the department's criterion for establishing priorities in construction and improvement projects unless the department is specifically instructed by the government to take these factors into consideration. If the

Cabinet decides that special attention should be given to a particular depressed region when determining priorities among projects, and a directive is issued to this effect, the department then gives serious consideration to the employment and other direct and repercussion effects of projects. But initially it is a political decision whether or not the economic state of areas should be given any weight in the departmental decision-making process in respect to expenditure programs.

While such analysis as is undertaken by the Resources and Development Division may yield information regarding program effects pertinent to fiscal policy, the analysis is conducted for purposes of evaluating projects and determining priorities from the point of view of securing adjustments in the allocation of resources. In this evaluation one project is given priority over another on the basis of such considerations as direct employment of resources, employment and income generated, and the economic conditions prevailing in the areas in which the projects are planned to be undertaken, only when other social and economic factors remain relatively equal between the two projects.

In instances when the economic impact of expenditures is considered important due to economic conditions, however, there is no framework by which that impact can be systematically analyzed. Under the present system spending and program effects can only be evaluated on an ad hoc and superficial basis.

Spending Effects

The logical framework for analyzing the impact of government

expenditures in terms of spending effects is a system of national accounts and related systems which depict the incomes and expenditures of various sectors and economic units in the economy. This would place the government expenditure program in the broad perspective of the economy as a whole and would indicate the interaction between the government sector and other sectors of the economy as well as between government and individual industries. While each system of accounts such as the national income and product accounts, and input-output and flow-of-funds data focuses attention on a particular function, they may be interrelated by the use of common concepts and definitions, thereby forming a homogeneous framework of accounts. Such a system of accounts may be referred to as the national economic accounts.

The present accounts of the Federal government cannot be readily integrated into the framework of National Accounts, as compiled by the Dominion Bureau of Statistics, and considered on the basis of these latter accounts. The detailed information on government expenditures as presented in the Estimates and Public Accounts is not consistent with the information on transactions in other sectors of the economy as presented in the National Accounts. Neither do the Public Accounts meet the demands for information for such purposes as placing the government sector within an input-output framework, which in Canada is based on National Accounting concepts to preserve consistency for analytical purposes. It is therefore difficult to consider government expenditures in terms of economic transactions between the different parts or units of the economy.

The estimates of goods and services purchased by government

as presently derived in the National Accounts is very unsatisfactory. The information in the National Accounts of transactions of government is derived from government budget documents. But very little information on the composition of government purchases of goods and services is included in these documents. The figure as presented in the National Accounts is a residual which is obtained by deducting from total budgetary expenditures all outlays which are not made directly to purchase new goods and services.⁶ Not only will any error in misclassification of the other items be reflected in the residual, but this method provides little information for analysis, so that any change in expenditure cannot be evaluated in a meaningful way.

The Standard Commodity Classification and the Standard Industrial Classification systems⁷, developed by the Dominion Bureau of Statistics form the basis of the National Accounts statistics. One of the problems of integrating government budgetary data with the National Accounts is that it is very difficult, if not impossible, to work the existing standard object classification applied in classifying government expenditures, into the Standard Commodity Classification of the National Accounts. The Standard Object Classification, while it does distinguish between office stationery and equipment, materials and supplies, etc., does not indicate what these categories consist of in terms of the categories of commodities under the Standard Commodity Classification. This is necessary for the industrial distribution of income and expenditures as shown in the National Accounts.

⁶ Canada, Dominion Bureau of Statistics, National Accounts Income and Expenditure, 1926 - 1956, (1962), p. 161.

⁷ See Canada, Dominion Bureau of Statistics, Standard Commodity

In other instances some of the object codes, such as "#20 Contributions, Grants, Subsidies, etc. Not Included Elsewhere", include in one code several types of economic transactions. These must be separated into economic categories for the purpose of analyzing spending effects. Furthermore, there is no service classification by which services may be classified.

In summary, the lack of any systematic analysis of the spending effects of government expenditures stems largely from the absence of an economic character classification of expenditures. The basis for an analysis of spending effects is a detailed classification of goods and services purchased under each program. Furthermore, such a classification of goods and services must be developed in line with the Standard Industrial Classification System which would indicate the spending effects on the basis of industries. There is also the question of spending effects by regional areas. The present classification scheme makes it virtually impossible to determine the spending effects of the total government expenditure plan, or of individual programs, and consequently the contributions they may make to production and income, and therefore employment goals, in the short-run.

The 1964 budget speech included for the first time, in an appendix and in the accompanying Budget Papers, an illustration of budgetary revenues and expenditures on the basis of the National Accounts. They did not include, however, an analysis of borrowing

Classification Manual (Ottawa: Queen's Printer, 1959), and Dominion Bureau of Statistics, Standard Industrial Classification Manual (Ottawa: Queen's Printer, 1960).

and lending and crown corporation operations, which have a substantial effect upon income and employment. Furthermore, the concentration is on aggregates which tends to overlook the problems of specific industrial sectors and regions of the economy.

There have occurred particular instances in the past where spending effects, such as the direct employment of labour, have been taken into consideration in the evaluation of expenditure projects. This has applied to specific projects introduced primarily to alleviate unemployment. In such cases the projects were required to be justified on other grounds as well as in respect to their employment content. The Treasury Board would examine the projects in the manner typical of its expenditure review process while leaving the aspect of the employment content to other government agencies. For example, during the fiscal year 1963 - 64 the government requested departments to submit supplementary estimates for projects that were to be introduced under a program designed to alleviate the problem of high seasonal winter unemployment. Treasury Board conducted its usual review of these projects, but it was left to the Department of Labour to examine the projects with respect to their employment content and employment generating capacity. Introducing the program to the House of Commons, the Minister of Labour, A. J. MacEachen, described it as follows:

I have been authorized by the government to ask various departments to bring forward additional projects for which moneys are not provided in the main estimates. . . . The item provides that these programs are subject to approval by treasury board, but I should like to add that they will also come forward to the Department of Labour for examination. The Department of Labour will attempt to assess the acceptance of these programs on two counts, first, that there be sufficient labour content or employment content in these programs to justify their acceptance as an employment measure; and second, that these projects be undertaken in areas of high unemployment . . . this is an effort to deal with unemployment by providing additional programs with a justifiable labour content

and to apply them in areas of high unemployment.⁸

The analysis of government expenditures conducted by the Financial Affairs and Economic Analysis Division of the Department of Finance is to a limited degree an analysis of spending effects as defined in this study in the sense that it is concerned with the short-term effects on income and production. But the analysis does not apply to individual programs and their effects on production by industry and their effects on employment. The Division is concerned primarily with the general effect on the economy of the total government expenditure program in terms of aggregate goods and services produced, capital accumulation, etc. and the requirements of the economy in terms of these aggregates. Analysis of the effects of transfers is limited to total transfers and type of transfers and does not apply to the effects of individual and specific transfers on the economy. Furthermore, the analysis conducted in the past has been to a large extent an ex-post analysis (i.e. what has taken place). With expenditure estimates placed on the basis of an economic classification it could become an ex-ante one.

The Financial Affairs and Economic Analysis Division is attempting to make use of econometric models to determine the requirements of the economy. Such tools of analysis and, in general, the type of analysis presently conducted are relatively new to the Division. Increasing attention, however, has been given to economic analysis and

⁸Canada, House of Commons, Debates, July 26, 1963, p. 2672.

new tools and techniques of analysis by this Division in very recent years, although it is handicapped by the lack of sufficient and adequate data on economic activity and economic developments, and the time lag in processing the statistical information that is made available.

In the past there has been very little liaison between the Treasury Board and Financial Affairs and Economic Analysis Division during the annual estimates review process by the Treasury Board.

Program Effects

It was submitted earlier that certain effects of expenditure programs which are likely to be taken into consideration in an objective analysis of the programs to determine their desirability from the point of view of securing adjustments in resource allocation would also be considered in an analysis of the contribution of the program to employment and economic growth. To the extent that use is made of forms of cost-benefit analysis in evaluating programs and establishing priorities within the department, some information regarding the contributions made by the programs, in terms of program effects, to fiscal policy objectives may be produced in the present process.

The analysis of long-term effects of various individual projects in the fields of natural resource development, primary industries, atomic energy, etc. is undertaken by departments working in close liaison with the Resources and Development Division of the Department of Finance. This analysis is primarily in respect to projects in their initial stage

of planning prior to their submission to the Cabinet for approval in principle. During a personal interview with officials in this Division it was asserted that formal cost-benefit analysis is applied to projects which readily lend themselves to this type of analysis, and that consideration is given to direct and indirect costs and benefits expected to accrue over a period of several years in the future. In areas where formal cost-benefit analysis is not applied, attempts are made to obtain as much relevant information as possible and decisions are made on the basis of this information and on judgments made by the analyst. There is no liaison, however, between this section and the Treasury Board at Estimates time.

In certain departments, particularly the Department of Northern Affairs and National Resources, there is evidence of increasing attention being given to the development of objective criteria for evaluating and justifying programs such as those pertaining to parks, water resource development, northern resource development, etc. For example, the department has established a program by which it contributes 50 percent of the cost of establishing or improving airstrips by private interests for development purposes. Certain criteria are required by which applications for the government's contribution under this program may be judged. Among the various factors taken into consideration in the past have been the area served, the type of and the extent of the resource being developed, the production plans of the party concerned, and the markets that have been negotiated for the resource which will determine production and give effect to production plans.

The Department of Transport also makes use of economic analysis

to a degree in planning capital projects such as the construction or improvement of an air runway and terminal. It takes into consideration such factors as the amount of traffic on the runway, the type of aircraft now using the runway and types expected to be using it five to ten years in the future, the amount of congestion at the terminal, cargo movements, etc.

In justifying various projects in relation to its harbours and rivers engineering services, the Department of Public Works considers various factors which it includes in its expenditure submissions to Treasury Board. For example, it may propose to reconstruct a wharf or provide a breakwater extension in a certain location. Its estimates submission may describe the project, including information concerning the geography of the area, the proximity of other similar facilities, the occupations of the people of the area, and the number of people and boats served.

The above types of evaluations and justifications, however, are undertaken on an ad hoc basis. Furthermore, the indications are that, in general, inadequate attention is given to program effects or the longer run effects of government expenditure.

In summary, the impact of expenditure programs on the economy from the point of view of fiscal objectives is secondary in the evaluation of the programs. No direct analysis is conducted by any agency in government of the contribution that government expenditures make towards the achievement of fiscal goals. Any light that may be shed on program effects stems from the analysis made of expenditures from the point of view of resource allocation. But even in respect to resource

allocation the planning and evaluation process is inadequate. Well developed long-term departmental planning of expenditure operations has been neglected in the past and is only now being given greater attention. The present scheme of expenditure classification and preparation does not identify objectives and accomplishments of expenditure activities which could conceivably give some indication of the probable effect of the activities on the economy from the point of view of employment and economic growth. Objective analysis in terms of cost-benefit analysis which includes repercussion effects is the exception rather than the rule. Analysis of spending effects is practically negligible.

To the extent that an analysis of budgetary expenditure programs in terms of costs and benefits, which may include program effects relevant to fiscal policy, is undertaken, it is conducted by agencies other than Treasury Board. This is also generally true of the analysis of programs introduced primarily as fiscal policy. The result is an unco-ordinated and non-systematic analysis of government expenditures in which reconciliation between the major purposes of budgetary policy becomes indeed difficult.

Other Limitations

Lack of Comprehensiveness

A limitation of the budget which is closely related to the analysis of the budget for its effect on the economy is that it is not as comprehensive as it could be. It was pointed out earlier that various government financial transactions do not appear in the

budget as expenditures and receipts; yet these non-budgetary transactions may play a vital role in influencing economic activity. The budgetary transactions are therefore only a guide to general policy rather than a complete indication of government fiscal intentions.

There are also the Crown Corporations, notably agency and proprietary corporations, whose financial transactions are excluded from both budgetary and non-budgetary transactions in the government accounts. The transactions of these corporations add up to a considerable sum and such corporations as the Central Mortgage and Housing Corporation, the Farm Credit Corporation, and the Industrial Development Bank, through their operations may contribute significantly to the promotion of employment and economic growth. Yet neither the amount nor the direction of their transactions is indicated in the annual budget presented to Parliament.

Rigidity and Time Lags

An inherent problem of fiscal policy is flexibility and timing. Should action be initiated as soon as possible when an upward or downward movement in the economy begins or is forecast, which may result in undesirable effects on employment and prices, or only after some delay? When a need for fiscal action is recognized, time is required to permit the formulation and initiation of a program by the government, and once the program has started, additional time is required before its economic effects are felt.⁹ Actions initiated in

⁹ For an account on time lags in the implementation of fiscal policy, see R. M. Will, "Fiscal Policy Time Lags", Report of Proceedings of the Seventeenth Annual Tax Conference, Canadian Tax Foundation, (Toronto, 1964), pp. 289 - 293.

advance of imperfectly foreseen disturbances may be de-stabilizing if the forecast is erroneous. On the other hand, delayed action will make the cumulative movement much more difficult to check. The complicated and rather lengthy process of formulating, authorizing and administering expenditure and revenue proposals contributes considerably towards making the Canadian budgetary system a rather inflexible one for implementing fiscal policy. Expenditure estimates are made from six to eighteen months before they are carried out. As K. W. Taylor, former Deputy Minister of the Department of Finance, has pointed out:

. . . our government has to make quite firm and usually rather inflexible decisions, between Christmas and Easter of each year which set the pattern of fiscal policy for the ensuing 12 months.¹⁰

Unless a very accurate method of long-range forecasting is developed it is difficult to determine economic conditions so far in advance.

At present the budget is more flexible for implementing anti-recessionary policies than anti-inflationary ones due to the fact that the main expenditure estimates are not final and a department may undertake additional activities, or extend its program in the activities and services to which it has already committed itself, during the course of the fiscal year by submitting supplementary estimates. Thus, should the economy suffer an unforeseen slump mid-way through the fiscal year the government is able to take steps to stimulate the economy by submitting supplementary estimates for additional expenditure programs. The budget is less flexible if the economy should suddenly experience an unanticipated inflationary spiral mid-way through the fiscal year.

¹⁰ J. J. Deutsch et al, The Canadian Economy: Selected Readings (Toronto: MacMillan Co., 1961), p. 292.

Expenditure programs are not easily postponed or stopped if they are already under way. Yet for the government to proceed with its planned programs would result in increased inflation as employed resources would have to be bid away from private activities, thereby increasing both factor and product prices.

Fiscal Policy and Political Considerations

Political considerations and pressures may often impose severe limitations on the utilization of fiscal policy. Given the conditions in the economy, programs which are appropriate from the point of view of their impact on the economy may be discarded in favour of programs with more political appeal. There may be pressures to increase government spending or to decrease taxes even in periods of full utilization of resources and inflationary tendencies. Furthermore, deficits and surpluses, which may be incurred in the budget as a result of the conscious use of expenditure and revenue programs to stimulate or control the economy, still often lead to charges of irresponsible finance. Because of various considerations and pressures of this nature, the budget presented in any given year may not always be the best economic plan with regard to prevailing or anticipated economic conditions.

As the economy grows and national product rises there is a tendency for government expenditures to rise also. It has been the practice in the past to spend most of the additional tax revenues generated by economic growth, and the result has been the postponement of debt and tax reductions. It is true that the government must have revenues for highly desirable programs and services and that public

demand for various government services is continually growing, but in times of economic prosperity when inflationary pressures tend to build up, non-urgent expenditures should be kept down to a minimum and not increased merely because the government expects a larger amount of revenue in the coming fiscal year and is subject to public pressure to extend its program.

The budget has generally become a tool for political gain in the hands of the government party during election years.¹¹ A usual sign of an impending election is a tax cut in the budget or an increase in certain transfer payments such as Old Age Pensions. This is the so-called "election budget". It may also include other vote catching provisions even though they could conceivably have an adverse effect on the economy. For effective use of fiscal policy a change of attitude is required, or, what has been described as, "a vision which looks beyond the next election, which puts lasting national benefits beyond political expediency"¹²

It is difficult to achieve fiscal goals by the use of such ad hoc policies that were characteristic of the post-war period. To await manifestations of economic instability and then attempt to reshape expenditure programs on a random and emergency basis is inadequate. It makes more sense to plan expenditure programs so that it may be possible to alter them to achieve the right effects at the proper

¹¹In 1957 the government was accused of not taking into consideration a report forecasting a decline in economic activity when the budget was prepared that year. The budget was presented shortly before the election of that year.

¹²Committee for Economic Development, Taxation For Growth (New York, 1957), p. 8.

time. Besides concern with temporary maladjustments there is also a need to look at the structure of the economy, to estimate the needs for balanced economic expansion and the effects of government expenditure policies in this respect and to gear fiscal programs to the fiscal objectives. With consideration given to the spending and program effects of departmental expenditure plans which extend beyond one fiscal year it is conceivable that fiscal policy could be made more effective in its implementation.

In conclusion, some type of framework is desirable which will provide the relevant quantitative data for the analysis of expenditure programs from the point of view of their impact on the economy. This would enable the government to determine the contribution made by its total expenditure program to fiscal objectives in the light of prevailing or forecast economic conditions. It would provide the basis for the systematic analysis of programs introduced as fiscal policy. Furthermore, it would permit a reconciliation between the objective of fiscal policy and other budgetary objectives.

IV

IMPLICATIONS OF PROGRAM BUDGETING FOR FISCAL POLICY

The program budget has been given considerable attention over the past decade in Canada and the United States as well as other countries. In its report on government administrative organization and procedure the Royal Commission on Government Organization in Canada, or what is known as the Glassco Commission, recommended the adoption of program budgeting.¹ As a result of the Commission's report various features of the program budget have been implemented in the federal government while others are presently being considered. From all indications it would appear that some form of program budgeting may be adopted in Canada. From the point of view of expenditure analysis this form of budgeting could overcome many of the limitations and inadequacies of the present system as outlined in the previous

¹The Glassco Commission's report, however, falls far short of a blue-print of detailed information for the establishment of program budgeting. Like its counterpart in the United States, the Hoover Commission, the Glassco Commission limited its report on this matter to an outline of some of the principles of program budgeting. The Commission emphasized administrative efficiency, that is, the establishment of techniques and procedures to carry out government operations in the most efficient manner. Developments following the Glassco report have also been in this direction with considerable attention being given to decentralization of authority and related management control and reporting schemes. See Canada, The Royal Commission On Government Organization (Ottawa: Queen's Printer, 1962), Vol. I, pp. 93 - 230.

chapter. It may also permit more active and effective use of fiscal policy.

A. The Program Budget²

General

Program budgeting departs from the traditional form of budgeting in form, technique, and outlook. In essence it is a form of budgeting which shifts the emphasis from the means of achievement to the ends or objectives to be achieved. In this respect it has been described by the Commission on Organization of the Executive Branch of Government in the United States (the Hoover Commission) as "a focus of attention on the ends to be served by government and continuous scrutiny and evaluation of them rather than on the dollars to be spent."³

²A distinction should be made between the terms "program budget" and "performance budget". They may be distinguished according to their time dimension. Program budgeting is forward-looking and involves the planning or projecting of government operations. Performance budgeting is concerned with past records of performance or accomplishment and the application of these performance units, or other devised performance measures, to current operations. A program budget might stop with broad program costs; it need not be extended to performance units. The two types of budgets may also be distinguished according to purposes served. As Jesse Burkhead has stated, the program budget "is useful for review and decision-making at and above the departmental level", while the performance budget is designed to serve "management purposes at and below the departmental level". For a more detailed account of the distinguishing features between these two types of budgets, see Jesse Burkhead, Government Budgeting (New York: Wiley and Sons, 1956), pp. 139 - 140.

³United States, Commission on Organization of the Executive Branch of Government (Washington: Government Printing Office, 1949), p. 36.

Following the Hoover Commission Report in 1949 program budgeting was implemented to a certain extent in the United States. In the budget expenditures are presented in the form of activities. Descriptions of the activities are included, and where feasible, so are the output data. R. N. McKean, however, has been fairly critical of the United States system of program budgeting. In his words "the current document falls far short of being an effective program budget." He submits that

Characteristics of the Program Budget

Classification of Expenditures by Functions, Programs, Activities and Projects

A principal characteristic of program budgeting is the classification scheme by which expenditures are presented, that is, on the basis of functions, programs, activities and projects. Few attempts, however, have been made to give precise definitions to these terms.⁴ This may be partly due to the fact that the scope of these categories of expenditures is a matter for judgment. Indeed, quite frequently even a general distinction between these terms by level of performance is not established with the result that there has been a tendency to use the terms synonymously to indicate types of government undertakings.

The terms function, program, activity, and project may be generally described as follows:

Function — a major division of governmental operations characterized by the common purpose to which the operations are directed such as national defence, natural resource development, transportation and communications, etc.

programs are presented in excessively broad terms with the result that "there is little hope of ever devising quantitative measures that would shed much light on the worth of such conglomerations." While programs are further broken down into activities, in many cases "these so-called 'activities' - e.g., pay and allowances, clothing, subsistence in kind, and travel - are really species of objects . . ." He submits that "the first step toward getting more useful exhibits is to put budget figures into categories that more nearly correspond to end-product functions." See R. N. McKean, "Evaluating Alternative Expenditure Programs", Public Finances: Needs, Sources and Utilization, Report of the National Bureau of Economic Research (Princeton: Princeton University Press, 1961), pp. 337 - 352.

⁴The Department of Economic and Social Affairs of the United Nations has attempted to define these terms. See United Nations, Department of Economic and Social Affairs, Report of the Workshop on Budgetary Classification and Management in Central America and Panama (E/CN 12/692, September 18 - 30, 1963) (New York, 1964), p. 77.

Program — a combination of operations or actions that yield distinguishable outputs or end-products or attain specified objectives. It is a partial means of accomplishing the purpose designated by the function.⁵

Activities and Projects — are subdivisions of a program and are particular methods of producing the output or achieving the objectives of the program, the project representing a sub-division of an activity.⁶

Concentration on Ends or Objectives

Another essential feature of the program budget is the emphasis placed on the objectives to be achieved, quantitatively measured where feasible, as well as the methods of achieving the objectives. It presents the purpose for which the funds are required and consequently what the public can expect from the use of these funds. As the Hoover Commission

⁵This interpretation is largely that presented by R. N. McKean. In attempting to define the term "program" McKean has commented: "A program is the counterpart of an 'industry' in the private sector of the economy — and is just as ambiguous, as hard to define, and probably as useful a concept — as an industry." See McKean, op. cit., p. 338.

The experience of the federal, state, and local governments in the United States has shown that the delineation of programs is quite arbitrary and that accomplishments may be measured at different levels of operation and in a variety of ways. See Burkhead, op. cit., pp. 158 - 181.

⁶A distinction between an activity and a project that is sometimes made is that the former represents a sub-division of an operating or current program, while the latter is a component of a capital program.

has stated, the program budget "gives more comprehensive and reliable information to the President, the Congress, and the general public, and helps the individual Congressman to understand what the government is doing, how much it is doing, and what the costs are."⁷

Not all program objectives, however, may be submitted to quantitative measurement even though they may be identifiable. In such cases a description of the program and what is expected to be achieved, together with its costs, must suffice.⁸ Most programs of this nature can be described fairly meaningfully.

Planning

Closely related to the establishment of objectives is the necessity of planning the programs, activities, and projects by which these objectives are to be achieved. This includes both short and long-term planning, indicating the total cost of a program, the length of time anticipated for its completion, and the amount proposed to be accomplished in the coming fiscal year. In program budgeting planning is generally undertaken on a systematic basis.

It would appear that planning is most realistically approached on a three to five year basis. During a period of this length the

⁷United States, Commission, op. cit., p. 37.

⁸Burkhead has termed this the activity-cost approach as distinguished from the end-product approach although his treatment of quantitative measurement of budgetary proposals relates to the more specific performance measurement extended to include unit costs and units of work per man hour. For a detailed account of performance measurement, see Burkhead, op. cit., pp. 133 - 181.

structure of the economy and technology are not likely to change drastically so as to disturb planned programs to any significant extent. Furthermore, the tenure of governments is usually from three to five years. A period of less than three years is generally too short to accomplish many objectives. On the other hand planning for periods in excess of five years brings in a considerable degree of uncertainty. The longer the period the greater the probability of unforeseen events. In fact, any type of planning is undertaken in the face of a fair degree of uncertainty of the future. Consequently, it would be desirable to have planned programs regularly revised every year in accordance with changing circumstances and conditions. This would provide a "rolling" three or five year plan based on up-to-date information and estimates. In this manner a certain amount of flexibility would be provided to meet unforeseen developments without abandoning the basic long-term program. As the Glassco Commission stated:

Having regard to the rapid elaboration of government activity and the continuing demand for the provision of new or enlarged programmes of public expenditure, the question of forward planning assumes major significance. Based upon forecasts by each department over a period of years ahead, surveys of total anticipated expenditure in relation to prospective resources would provide a most useful background against which decisions involving substantial future expenditures should be taken. A five-year projection, amended and updated each year, should be an indispensable tool for policy-making.⁹

Criteria Application

Some type of criterion is essential to permit a rational choice to be made between competing programs. To the extent that accomplishments may be objectively appraised, the presentation of programs and projects

⁹Canada, Royal Commission, op. cit., pp. 101 - 102.

in terms of accomplishments or end-products facilitates the application of criteria for purposes of evaluating alternative expenditure proposals and establishing priorities. Given the expected achievements and the total costs of the programs as previously described, costs and benefits may be evaluated to determine the desirability of a program. On this matter R. N. McKean has stated:

. . . one can not properly plan expenditures on the basis of either cost alone or needs alone. There is no budget size or cost that is correct regardless of the payoff, and there is no need that should be met regardless of cost. One has to make judgments about both costs and gains. What we should like, therefore, in evaluating alternative expenditures, are estimates of both costs and gains. Or, where estimates cannot be in terms of a common denominator, we should like at least relevant clues to both costs and gains so that more informed judgments about them can be made.¹⁰

A number of criteria may be applied for the purpose of evaluating programs and establishing priorities, using analysis of costs and benefits. Among the yardsticks that may be used are cost-benefit ratios and the maximization of gains minus costs, the latter stemming from marginal cost and marginal gain analysis.¹¹ With regard to cost-benefit ratios, having arrived at an acceptable cost-benefit ratio as a yardstick, the problem that remains is to evaluate the cost and the benefits of programs and accept only those with a ratio greater than or equal to the one established. Those programs with the largest ratio would be given priority. Using marginal analysis, on the other hand, with the criterion being the maximization of gains minus costs, each program would be pushed to the

¹⁰McKean, op. cit., pp. 337 - 338.

¹¹For one approach to the problem of evaluation of government programs by the use of marginal analysis, see D. M. Winch, The Economics of Highway Planning (Toronto: University of Toronto Press, 1963).

point where marginal costs are equal to marginal gains. If a given amount of resources may be put to one of several uses, the one with the largest net gain would be given priority. In cases where objectives are fixed and there are several methods of achieving the objectives, that method should be chosen which minimizes the cost of achieving the objective.¹²

Progress Review

The inclusion of long term programs in the budget enable a progress review to be conducted during the annual presentation of the budget. The cumulative and the remaining costs may be shown together with an indication of the accomplishments. This may also be extended to a requirement that the operating units submit regular progress reports to the departmental decision-making authorities and to the central financial control agencies showing the current standing of their programs and resources in relation to existing plans and policies.¹³

¹²In the process of applying criteria care must be taken that subcriteria employed in evaluating projects under a program are consistent with the higher-level objectives and criteria of the program, and that the overriding goals are not lost sight of while pursuing piecemeal objectives. This process of choosing among different courses of action is one of sub-optimization in which problems are broken down into sub-problems to which quantitative analysis may be applied to help find solutions. For instance, if the criterion applied to the objective of a program is to maximize the value of output minus costs, then the criterion to be used in evaluating the methods (projects and activities) of attaining the objective must also take the form of maximum net value of output. For a more detailed analysis of the problem of sub-optimization, see R. N. McKean, Efficiency In Government Through Systems Analysis (New York: Wiley & Sons, 1958), pp. 29 - 34.

¹³A periodic, detailed examination of all phases of the work of an organizational unit, that is, an appraisal of the utilization of personnel, materials, methods, and management techniques in relation to expenditures is known as an operations audit. Such a detailed

The advantages of the program budget are readily apparent.

With regard to resources allocation it is designed to shift the attention of the central financial control agency and the legislature from pre-occupation with the individual details of expenditure to the identification, program by program, of the operations of government departments and to the purposes and objectives of expenditures as well as the results achieved. While items purchased are still of significance for purposes of determining spending effects, under the program budget the items would be identified with what the government is doing and what it expects to accomplish. In general, this type of budget is better designed to provide meaningful information for decision-making at the administrative, executive and legislative levels of government.¹⁴

B. Expenditure Determination and Analysis: Relevant

Features of Program Budgeting For Fiscal Policy

The features of program budgeting which would appear to facilitate

examination, however, is more appropriately reserved for a performance budget. See Supra, p. 87n.

¹⁴For those interested in pursuing the subject of program and performance budgeting further in respect to its accounting and administrative aspects, see Jesse Burkhead, Government Budgeting (New York: Wiley & Sons, 1956), pp. 110 - 181; F. C. Mosher, Program Budgeting: Theory and Practice With Particular Reference to the United States Department of the Army (Chicago: Public Administration Service, 1954); Gladys Kammerer, Program Budgeting: An Aid to Understanding (Gainesville, Fla., 1959); United Nations, A Manual For Programme and Performance Budgeting (New York, 1961); A. E. Buck "Performance Budgeting for the Federal Government", Tax Review, (July 1949), pp. 33 - 38; D. S. Burrows, "A Program Approach to Federal Budgeting", Harvard Business Review, (May 1949), pp. 272 - 285; Carlos San Pedro, "Performance Budgeting in the Philippines", Canadian Public Administration, VI, 1963, pp. 313 - 330; R. N. McKean, Efficiency In Government Through Systems Analysis (New York: Wiley & Sons, 1958), pp. 247 - 309; and Arlene Shadoan, Preparation, Review and Execution of the State Operating Budget (Lexington: Bureau of Business Research, 1963).

an assessment of spending and program effects of government expenditures and the employment of fiscal policy are:

- (i) the nature of the expenditure accounts,
- (ii) concentration on quantitative analysis, and
- (iii) the planning function.

Expenditure Accounts

The classification of expenditures by clearly identified programs and component activities and projects would permit an analysis of the impact of expenditures on the economy by individual programs and projects. A specific and detailed analysis could consequently be conducted as well as an analysis on an aggregate basis. The classification of expenditures in the form characteristic of program budgeting is insufficient in itself for fiscal policy analysis, but it is an essential and basic step in the direction of establishing a system which would facilitate such an analysis. The identification of the objectives to be achieved in terms of resource allocation and public needs for each individual program and project would furthermore permit a reconciliation between fiscal policy and resource allocation goals.

Quantitative Analysis

Program budgeting, with its emphasis on objective criteria for expenditure evaluation, establishes the outlook toward analysis which is required for determining program and spending effects. An evaluation of expenditure programs on the basis of objective criteria requires quantitative data. The systematic provision and utilization of such data which is inherent in program budgeting establishes the framework

for the determination of the program and spending effects of expenditures. As previously mentioned, certain data provided in the process of evaluating expenditures from the point of view of resource allocation would most likely be of significance for the analysis of these effects, particularly program effects. The data or information provided could also be extended to include data pertinent for the analysis of spending and program effects.

Systematic quantitative analysis of all programs to which such analysis is applicable would automatically be applied to programs introduced as fiscal policy. Since the criterion is related to the outlined objectives, obviously the criterion for fiscal policy programs would be developed and applied accordingly.

Planning Function

Basic to program budgeting is the requirement that planning, whether at the program level or the more specific project level and whether long or short-term, be established on a formal basis. Formal planning documents encompassing departmental expenditure programs for a period of three to five years would be of substantial value for fiscal policy implementation. They would serve to diminish the administrative difficulties of effecting changes in the rate of implementation of activities and projects within the program as economic conditions demand. This would provide increased flexibility of the budget for fiscal policy purposes to the extent that fiscal policy may be undertaken without going through the time consuming process involved in the formulation and authorization of new programs and projects. As was already pointed out, the "rolling" type of plan would also make expenditure

programs more flexible thus permitting adjustments as economic conditions warrant.

In general, in view of the above features of program budgeting it is submitted that the adoption of this type of budget would contribute towards the establishment of a framework for analyzing the impact of government expenditures on the economy. It would also facilitate the active utilization of fiscal policy.

V

PROGRAM AND SPENDING EFFECTS: SUGGESTED

SCHEME FOR ANALYSIS

A. Form of Expenditure Accounts

For purposes of determining the program and spending effects of government expenditures it is proposed that expenditures be organized within the framework of the program budget and integrated with an economic character classification scheme. The classification scheme resulting from this integration will be termed a program-economic classification of expenditure.¹

Program Classification

In program budgeting the classification scheme is generally designed to serve the budgetary purpose of securing adjustments in the allocation of resources. It is designed to present information concerning government expenditures in a more meaningful form and in this manner to facilitate budgetary decision-making. But this type of classification is also significant for purposes of fiscal policy in the sense that it provides a framework for the analysis of the economic

¹The concept of a program-economic classification of government expenditures is not new. The classification of expenditures by programs and by the economic nature of the expenditures has been suggested by Richard and Nancy Ruggles, Gerhard Colm, and by the National Bureau of Economic Research. See United States, Congress, Senate, Joint Economic Committee, Federal Expenditure for Economic Growth and Stability, Papers Submitted by Panelists appearing Before the Subcommittee on Fiscal Policy

impact of specific government operations directed towards the achievement of identified objectives in respect to resource allocation and public needs. Furthermore, it facilitates a reconciliation between these two major budgetary purposes.

The delineation of programs and activities is a matter for judgment and is generally quite arbitrary. Basic to program formulation, however, is the requirement that programs be presented in a form such that the objectives or ends can be identified and that activities and projects, representing ways and means of achieving the program objective, be outlined in a form which will readily indicate what the government is doing to achieve the objective. The details of the activities and projects would indicate the accomplishments of government in any one fiscal year. In addition to these basic requirements the program classification scheme proposed in this study includes two other conditions designed to serve fiscal policy purposes. These are as follows:

- (1) Government operations of a capital nature should be presented as projects separate from those of an administrative or operational nature. It is the capital projects which are more readily altered to meet changing conditions and which, on the expenditure side of the budget, have the most significant direct spending impact on the economy.

(Washington: Government Printing Office, 1957), pp. 433 - 443; 483 - 492; and National Bureau of Economic Research, The National Economic Accounts of the United States, A Report by the National Accounts Review Committee of the National Bureau of Economic Research (Washington: Government Printing Office, 1957), esp. pp. 75 - 84.

- (2) To the extent that the considerations of program budgeting permit, programs, activities, and projects should be identified to the greatest extent feasible in the budget accounts by geographical region to facilitate the analysis of regional impact in tracing the effects of government expenditures on the economy.

The present operations of the Federal government, including the operations of crown corporations, may be classified under six functions: national resources and primary industry; transportation and communications; finance and commerce; national defence; social services; and general government and justice. Program budgeting does not require that government administrative units, such as departments, be organized on the basis of functions, but it is desirable for administrative purposes that all operations pertaining to a particular function are under the jurisdiction of the departments primarily responsible for the one specific function. To achieve this under the present organization in the federal government would require various transfers between departments and agencies.

Table V - I consists of an illustration of the manner in which government operations may be classified in the form characteristic of the program budget using the transportation and communications function as an example. The government department primarily responsible for this function is the Department of Transport. As illustrated, its operations may be classified into seven broad programs. These programs are in turn subdivided into various sub-programs on the basis of more specific objectives and services for purposes of facilitating activity planning and evaluation. The sub-programs are subsequently divided into component

activities and sub-activities and projects.² In a similar manner the operations of agencies and crown corporations which are concerned with the transportation and communications function may be broken down on the basis of programs and activities. This would result in a comprehensive presentation of all government operations in this area.

This classification scheme, besides possibly serving various budgetary administrative and control functions,³ would, from the point of view of expenditure analysis, serve to identify the various operations of government. It would also indicate the anticipated accomplishments in the current fiscal year, the coming fiscal year, and the following four years, and would indicate government plans and the general direction of expenditures over a seven to ten year period.⁴ In regard to this longer

²For an example of an alternative form of breaking down the operations of the Department of Transport into programs and activities, see Canada, Royal Commission On Government Organization (Ottawa: Queen's Printer, 1962), Vol. I, pp. 184 - 206. For other illustrations of program and activity classification of various functions of the United States government, see United States, Commission on Organization of the Executive Branch of Government (Washington: Government Printing Office, 1949), and R. N. McKean, Efficiency In Government Through Systems Analysis (New York: Wiley and Sons, 1958), pp. 292 - 309.

³For an account of the process of allotting funds on the basis of programs and activities, delegating authority on this basis, and other administrative aspects of program budgeting, see Canada, Royal Commission, op. cit., pp. 96 - 206, and the literature on program budgeting outlined in Supra, p. 94n.

⁴Long-term plans regarding the objectives or programs of a department, if prepared on a seven to ten year basis, would provide the guides for shorter-term operating plans at the activity, sub-activity, and project level. The short-term operating plans, translated into resource and financial requirements, would provide the basis on which expenditure estimates would be prepared. In the estimates preparation and review process the expenditure estimates of the sub-activities and projects could then be related to the long-range programs which have been developed by the department. In other words, the estimates preparation and review process would be related to long-range planning.

TABLE V - I

CLASSIFICATION BY PROGRAMS, ACTIVITIES, AND PROJECTS

AN ILLUSTRATION

Function: Transportation and Communications

Department: Transport

- Programs: 1. Departmental Administration
2. Navigation and Marine Services
3. Civil Aviation
4. Road and Highway Development
5. Railroad Regulation and Assistance
6. Meteorological Service
7. Telecommunications and Electronics

2. Navigation and Marine ServicesSub-Programs: 2.1 Waterway Development^a

2.2 Marine Safety

2.3 Transport and Supply

2.4 Regulation and Control

2.1 Waterway Development

<u>Activity</u>	<u>Sub-Activity or Project</u>	<u>Expenditure</u>
2.11	Channel and harbour facility development	Current Capital
	2.111 Coastal harbours and channels	
	2.112 St. Lawrence River and Great Lakes harbours and channels	
	2.113 Inland waterways	
2.12	Research	

TABLE V - I -- Concluded

2.121 Engineering surveys

Activity by Accomplishment and CostExpenditure2.111 Coastal harbours and
channels (details)

CY NY NY+1 . . . NY+4

CurrentRegulation of canals,
administration of govern-
ment wharves and public
harbours, operation of
locks, collection of
tolls, etc. -----

CY NY NY+1 . . . NY+4

CapitalCanso Canal, N.S.
(Improvement)

Dredging -----

Retaining wall -----

Launchway -----

Landscaping -----

Related dwellings and
equipment -----

St. Peters Canal (N.S.)

Waterway DevelopmentSeven to Ten Year Program(General description and factual information where
possible)^aThis category includes the operations of the Department of Public
Works in this area.

term planning process, in certain areas of government, such as the field of waterway and resource development, fairly definite long-range plans and programs may be established. In other areas such as marine safety, however, which is predominantly of an operative nature, it would appear that the best that can be hoped for is some indication of the developments expected and the general activities that might be undertaken to improve facilities providing safety measures for navigation.

Economic Character Classification

Economic processes in an economy, such as the production of goods and services, are recorded in terms of transactions which take place between the different parts or units of the economy, that is, the money flows which occur in exchange for goods and services. The result is a system of national economic accounts which sets out the features of the economy and which is essentially a statistical framework for studying the structure and behavior of the economic system.

Transactions in an economy may be generally classified into sectors such as the personal sector, the business sector, and the government sector. In each of these sectors the transactions may be set out in a more detailed classification scheme. Expenditures in the government sector may be divided into current and capital expenditures, each group in turn being subdivided into categories such as expenditures on goods and services, transfers, interest, subsidies, etc. This division of expenditures is frequently referred to as an economic character classification in that it indicates the economic nature of the

expenditures.⁵ A more detailed classification under these categories would provide the practical basis on which the effects of government activity on the economy may be analyzed. It may be extended to a classification by industry and region. A classification by industry is essentially a classification by operating units or organizations (firms) associated with a commodity or service or with a group of commodities or services, the basic element of the classification being the commodity or service.

An economic character classification scheme for government expenditures is necessary to provide the data or information required for determining the effects of these expenditures on the economy. Such a scheme, however, must be consistent with the scheme developed to record the transactions of the economy as a whole if government transactions are to be viewed in relation to the transactions of other units within the economy. In conforming with this requirement the proposed economic character classification, as illustrated in Table V - II, is based on the concepts used by the Dominion Bureau of Statistics in recording economic transactions and compiling the National Accounts.

In this broad classification scheme expenditures are divided into current and capital expenditures. The expenditures on current account are categorized into expenditures on goods and services, various transfer payments, and loans. Expenditures on capital account are shown for new construction and new machinery and equipment, the

⁵For a detailed account of the economic character classification see United Nations, Department of Economic and Social Affairs, A Manual For Economic and Functional Classification of Government Transactions (ST/EAC/49, 1958) (New York, 1958); and Jesse Burkhead, Government Budgeting (New York: Wiley and Sons, 1956), pp. 212 - 243.

purchase of existing capital assets, the purchase of land, various capital transfers, and loans for capital formation purposes.

It is proposed that expenditures on goods and services be classified in detail in accordance with the classification schemes developed by the Dominion Bureau of Statistics. The Bureau classifies goods on the basis of its Standard Commodity Classification which categorizes commodities into 5,622 classes, 498 groups, 82 divisions and 5 sections. Appendix E, Table E - I illustrates the sections and divisions of the Standard Commodity Classification and gives a sample illustration of the classification by groups. The Bureau has also developed a tentative classification of services which is to serve as the basis for classifying services in the economy. This service classification is illustrated in Table E - II.

It would appear that the classification of expenditures on goods by divisional groups, that is, at the two-digit level, is adequate for the purpose of analyzing the impact of expenditures on the economy in the sense that it would yield sufficient information regarding the types of goods purchased by the government. Similarly the classification by the 43-odd service divisions would be sufficient to show the type of services on which expenditures are made by the government. It is proposed that these two classification schemes comprise the detailed section of the economic character classification scheme to indicate types of goods and services purchased.

The logical sequence to this scheme is to identify expenditures on goods and services, transfer expenditures, capital expenditures, and

TABLE V - II

GENERAL ECONOMIC CHARACTER CLASSIFICATION*

Current Account

1. Current expenditures on goods and services
 - (i) Goods - classified according to the Dominion Bureau of Statistics Standard Commodity Classification.
 - (ii) Services - a classification of services as developed by the Bureau of Statistics.
2. Transfer payments to persons
3. Interest on the public debt
4. Transfers and subsidies to industry
5. Transfers to other levels of government
6. Transfers to federal agencies, enterprises, boards, commissions, etc.
7. Transfers to reserves
8. Transfers to abroad
9. Loans to private sector

Capital Account

1. New Construction
 - (a) Dwellings
 - (i) Contract work
 - (ii) Own account work (classified according to the Standard Commodity Classification and Service Classification as shown for current expenditures on goods and services)
 - (b) Other Buildings (by type)
 - (i) Contract work
 - (ii) Own account work

TABLE V - II-- Concluded

(c) Engineering Construction (by type)

(i) Contract work

(ii) Own account work

2. New Machinery and Equipment

3. Purchases of existing capital assets

(a) Dwellings

(b) Other buildings (by type)

(c) Other structures (by type)

(d) Used machinery and equipment

(i) Domestic

(ii) Imported

4. Purchase of land

5. Transfers to capital account of domestic sectors

(a) Other levels of government

(b) Federal agencies, enterprises, etc.

(c) Industry

6. Capital transfers to abroad

7. Loans to domestic sectors

8. Loans to abroad

*This classification scheme is based partly on a scheme developed by the Dominion Bureau of Statistics and schemes presented in United Nations, Department of Economic and Social Affairs, A Manual For Economic and Functional Classification of Government Transactions (ST/ECA/49, 1958) (New York: 1958).

loans with industries to determine the industrial sectors affected by government expenditure.⁶ This may be achieved by the use of the Standard Industrial Classification scheme developed and used by the Dominion Bureau of Statistics in compiling expenditure and production data on the basis of industry.⁷

This economic character classification scheme has been developed on the basis of the national accounting concepts and classifications used by the Dominion Bureau of Statistics in compiling the National Accounts. As a result it may be readily integrated with the national accounts and would facilitate the computation of national product, personal income, and the many other compilations regarding sector accounts shown in the National Accounts. For instance, the division of capital expenditures between purchases of land, previously existing assets, and new assets is necessary for determining national product. The purchase of land and existing assets does not represent current production and is therefore excluded from the measure of gross national product. Imports of used machinery and equipment on the other hand are included in capital formation in gross national product since they are additions to Canada's total stock of capital.⁸

⁶In respect to the usefulness of a classification by industry the United Nations has stated: "A classification by industry . . . would make it possible to determine, for example, the amount of goods and services purchased by the government from different industries, as well as the government contribution to capital formation in the various industries, directly, or indirectly by way of loans and capital grants to the private sector." United Nations, loc. cit., p. 37.

⁷See Appendix E, Table E - III, and Dominion Bureau of Statistics, Standard Industrial Classification Manual (Ottawa: Queen's Printer, 1960).

⁸For a detailed discussion of the conceptual framework of the Canadian National Accounts and a systematic description of the theoretical

Integrated Classification

Individually a program classification and an economic character classification serve distinct purposes. A classification by programs and activities is generally viewed in terms of facilitating the planning and evaluation of governmental operations which are undertaken to secure adjustments in the allocation of resources. A general economic classification serves the purpose of indicating the impact of aggregate government expenditures on the economy. It does not, in itself, provide information regarding the effects of individual governmental operations on the income and production, and consequently employment, of industrial sectors and geographical regions. This study attempts to develop a scheme which would provide such information.

It has been proposed that government expenditures be classified by program, activity, and project to identify specific governmental operations and, where possible, to indicate the regions in which they are undertaken. An economic character classification has been proposed, based on national accounting concepts, which is extended into a detailed economic classification of expenditures related to industries. It is now proposed to integrate these two classification schemes.

It is proposed that following the establishment of the program classification scheme the economic character classification in all its details be applied to the expenditures relating to the individual programs

constructs and definitions used, see Canada, Dominion Bureau of Statistics, National Accounts Income And Expenditure 1926 - 1956 (Ottawa: Queen's Printer, 1962), pp. 103 - 185.

and their components. The component activities, sub-activities, and projects would in this way be identified by their economic character. Expenditures of a capital nature would be shown separately which would serve to indicate the government's contribution to capital formation in the economy. The classification of transfers on the basis of the program-economic classification scheme would serve to identify the various types of transfers and the purposes for which they are made. Subsidies and loans made to specified industries and agencies for specific purposes would be described from the point of view of their direction and purpose. The presentation of expenditures on goods and services for both current and capital programs on the basis of standard commodities and services would provide information regarding the type and quantity of resources required to carry out the program and its component activities and projects. As illustrated in Table V - I this type of information regarding direct manpower and material requirements would be presented for government operations on a one to five year basis. This should not be too difficult as departments were to a certain extent concerned with this type of information for purposes of compiling estimates on the basis of the standard objects of expenditure.

In regard to expenditures on goods and services the manner in which material requirements for individual activities and projects could be classified according to the Standard Commodity Classification is illustrated in Table V - III. Service requirements are classified in a similar manner in accordance with the service classification scheme. These commodity and service requirements are then related to the Standard Industrial Classification by Industry Group. The estimate at current prices of the amount to be spent on commodities and services for a five

COMMODITY SERVICE AND INDUSTRIAL CLASSIFICATION

OF EXPENDITURES FOR INDIVIDUAL PROJECTS

Project: Genes Genes N.S. (T. 1000000000)

Construction (Own Account Work)

year period in the future for proposed or already approved projects will only be an approximation due to the possibility of price changes. There is also the possibility of miscalculations of resource requirements for a project. Such estimates should, however, give a fairly close approximation of the type and value of resources required, which, related to the Standard Industrial Classification, will indicate government requirements by industrial sector.

B. Analysis of the Impact of Various

Types of Expenditure

The program-economic classification of government expenditures has been proposed to provide information relevant to an analysis of the impact of individual government operations on the economy, and to serve as the basis for the analysis and employment of actions constituting fiscal policy. It has been emphasized that the impact of an expenditure program on the economy may be in the form of spending effects or program effects or both.

Spending Effects

In regard to spending effects, economic analysis is concerned with how economic units are directly affected by government expenditures and changes therein, and how these effects are in turn transmitted to other units or entities in the economy.

Expenditures on goods and services

Expenditures on goods and services are of a current and capital nature. The program-economic classification scheme is designed to yield information concerning the direct manpower, service, and material requirements for every individual activity and project undertaken by the government.

The type and value of services and materials purchased by government for any one fiscal year over a five-year period is identified with industries. The additions to the incomes of various industries as a result of government operations which involve the use of goods and services can consequently be readily determined. On the limiting assumption that industry increases its production and employment by the amount required to meet the demand by government for materials and services, the effect on production and employment in industry may be assessed.⁹ Information regarding direct employment in terms of personnel employed by government on a permanent or casual basis would also be indicated. To maintain a standard classification of employment, government employees could be classified in accordance with the occupational classification scheme established by the Dominion Bureau of

⁹As an illustration of the determination of the direct spending effect of government expenditure on employment, consider the following simplified example. Suppose the government undertakes Project A during the course of a given fiscal year. Assume fixed technical coefficients of production. Also assume that the government demand for goods and services of Industry i is met by an increase in current production rather than through inventory change. Let

X_i = total value of goods and services currently produced by Industry i .

M_i = manpower currently employed by Industry i (man-years).

M_g = manpower employed directly by the government on Project A (man-years).

On the basis of current production and employment in Industry i , an employment coefficient may be calculated as $M_i/X_i = m_i$. The classification scheme illustrated in Table V - III would yield information regarding the value of goods and services purchased by the government from Industry i . If government demand for the product of Industry i is denoted by x_{ig} , then employment resulting from this demand would be $x_{ig}m_i$. Total direct employment Y resulting from government expenditure on Project A would therefore amount to

$$Y = M_g + x_{1g}m_1 + x_{2g}m_2 + \dots + x_{ng}m_n$$

or

$$Y = M_g + \sum_{i=1}^n x_{ig}m_i$$

Statistics which lists 12 major occupational divisions and 273 occupation classes.¹⁰

In the capital account section of Table IV - II it will be noted that capital expenditures are of two types, namely "Contract Work" and "Own Account Work." With regard to capital projects which the government undertakes directly with its own facilities there would be no problem in determining the type and amount of resources used for the project on the basis of the standard commodity classification. Projects undertaken by contract would not present any difficulties in this respect either, as estimates are generally made by government departments concerned regarding material requirements when the cost of a project is first being determined.

It is recognized that, from the point of view of regional effects, invariably it is difficult to determine precisely on which regional industrial sector a program or project would have its most significant direct impact. The import content of the program, in terms of the materials brought in from outside the region in which it is undertaken, would have to be taken into account. There is the possibility that the direct spending effect may be primarily in another region or may even be outside the country.

In addition to the direct spending effects of government programs involving the use of goods and services, there are also indirect spending effects. An analysis of the indirect spending effects, however, would require inter-industry data to determine what

¹⁰ See Dominion Bureau of Statistics, Occupational Classification Manual, Census of Canada, 1961, (Ottawa: Queen's Printer, 1961).

effect the purchase of goods and services from Industry I will have on other industries. As Industry I increases its production to meet an increase in the demand for its product, it will require as inputs the outputs of other industries. To determine the indirect requirements for materials or labour in the interdependent productive system it is necessary to follow such requirements through a chain of successive inputs.¹¹

On the basis of inter-industry data, it is possible to construct production or industry coefficients which would indicate the combined direct and indirect spending effects on various industries of certain types of government projects, such as building construction, canal and harbour construction and similar engineering works, road construction, etc. The Harvard Economic Research Project has conducted exploratory studies in applying input-output analysis to the question of counter-cyclical employment generation. This has consisted of the calculation of ratios of employment to expenditure (man-years per thousand dollars of expenditure) for various types of expenditure programs.¹² Given

¹¹For a mathematical exposition of the method in which inter-industry flow data may be employed to determine the effect on production and employment which may result from a change in the demand for the product of one industry, see Appendix F. Essentially, in tracing these effects, use is made of the inverse matrix $(I - A)^{-1}$, which is sometimes termed the matrix multiplier. The matrix $(I - A)^{-1}$ represents the total output of each industry resulting from the production of a dollar's worth of final output of an industry. A $(I - A)^{-1}$ matrix for Canada is presented in the Dominion Bureau of Statistics, Supplement to the Inter-Industry Flow of Goods and Services, Canada 1949 (Ottawa: Queen's Printer, 1960).

¹²The results of the Harvard Economic Research Project indicated that, among the various types of government expenditure, those that generated the greatest amount of direct and indirect employment in terms of man-years per thousand dollars of expenditure included conservation and development construction, highway maintenance, residential and institutional construction, and water and sewage maintenance

such labour coefficients the employment generated by various types of government expenditures can be determined. It would be useful to extend this type of analysis to determine employment coefficients for individual industrial sectors with the consequence that, given a depressed industrial sector, those types of programs or projects may be introduced which have their primary spending effects in this sector. A limited factor in such analysis is that it is concerned with labour in the aggregate. The type of labour employed is as significant as the quantity. This technique of analysis could conceivably be extended to consider types of labour utilized by the construction of detailed production accounts for various commodities produced.

The above type of analysis on the basis of inter-industry data excludes the additional income and employment that may be generated by the respending of wages, salaries, profits, etc. received by the income recipients of the primary sequence. Such secondary effects are covered under the conventional multiplier principle. An average multiplier, in the conventional form, for government expenditures in general would indicate secondary effects on income as a result of the respending process. It would be desirable to take into consideration the conventional multiplier effects resulting from the initial increase in wages and salaries to determine the total income and employment generated.

construction. For an account of the techniques employed in this study, and the results achieved, see A. M. Strout, "Primary Employment Effects Of Alternative Spending Programs", The Review of Economics and Statistics, XL (November, 1958), p. 319 - 328. Using the inter-industry flow table of goods and services prepared for 1949 by the Dominion Bureau of Statistics, H. H. Binhammer has conducted a similar study of the employment generated by residential construction in Canada. See H. H. Binhammer, "The Fiscal Implications of a Housing Program," Canadian Journal of Economics and Political Science XXIX (August, 1963), pp. 336 - 347.

In essence, while the program-economic classification scheme would provide information in respect to the analysis of direct spending effects of programs employing resources, the evaluation of indirect effects would require data such as that presented in inter-industry tables. The inter-industry datum that has been provided in regard to the Canadian economy, however, is outdated. Input-output tables were constructed by the Dominion Bureau of Statistics using 1949 production data and were published in 1956.¹³ At present the Bureau is working on an up-dated input-output table, but its completion is not anticipated for some time.

The inter-industry flow table of goods and services for Canada is composed of 42 industries classified according to the Bureau's standard industrial classification scheme. It is an open input-output system in which the final demand sector is exogenous and is composed of households, business, government, and exports. The government sector, which is of primary interest here, shows government expenditures on goods and services as final demand as they appear in the National Accounts, although the details of the various government expenditures as final demand are shown in the table according to the industry in which the particular government establishment was classified.¹⁴

¹³A supplement to this publication was issued in 1960 which incorporated certain changes. See Dominion Bureau of Statistics, The Inter-Industry Flow of Goods and Services, Canada, 1949, (Ottawa: Queen's Printer, 1956), and Supplement to the Inter-Industry Flow of Goods and Services, Canada, 1949, (Ottawa: Queen's Printer, 1960).

¹⁴Government final purchases as shown in the inter-industry table are explained as follows: "The final output category 'government expenditure on goods and services' is shown as having purchased all the output of the public administration and defence industry plus those portions of the output of the transportation, communication, wholesale trade and community service industries which were produced by establishments whose

The Canadian input-output table was constructed by estimating the inputs into each industry rather than by estimating the disposition of output of each industry. It was necessary to determine the value of the various commodities and services used as inputs by an industry and then to determine the industry of origin. The basis of the figures for intermediate input for the federal government was the objects of expenditure of the Estimates. These objects are inadequate for this purpose, however, for it is difficult to translate the objects into an industry-of-origin classification. It is submitted that the proposed classification scheme outlined earlier would greatly alleviate this problem. For example, in regard to the construction industry in which government construction is placed, the proposed classification scheme would indicate the industry of origin of the various materials used in construction and on which expenditure was made.

In general, such information as would be provided by the proposed classification scheme would prove to be very useful if any attempt is made to introduce additional refinements in the government sector in inter-industry flow tables. While this may require more detailed information than that provided by the two-digit commodity classification which is illustrated in Appendix E, such detailed information would not be required on an annual basis. On the occasions that more detailed data are required, departments could

expenditure is included in 'government expenditure on goods and services' in the National Accounts Since all construction is assumed to have been put in place by the construction industry, capital expenditure on new construction is shown as being purchased from the construction industry." Ibid. Supplement. pp. 43 - 44. For a detailed description of Canada's 1949 input-output table and the methods used in compiling it, see Ibid.

be requested to submit estimates of commodities and services purchased on the basis of the three-digit classification.

Transfer Payments

Transfer payments, both on current and capital account, are classified in terms of the recipients of the payments as shown in Table V - II. Major transfer payments such as those found in the Department of Health and Welfare may be regarded as programs in themselves or sub-programs or major activities. In the planning and review process they would be considered accordingly. As far as the impact of these transfer payments on the economy is concerned, the direct income effect of transfers to persons is readily indicated, and the indirect effects in the aggregate can be estimated on the basis of the conventional multiplier principle. Beside an average multiplier of the conventional type, multipliers may be developed for different types of government expenditure. This would be desirable since various transfer payments are directed towards different groups which may have dissimilar spending habits.

Transfers, subsidies, and loans to industries on the other hand may be analyzed in terms of contributions to capital formation and the effect on the production and prices of the goods and services of the individual industry concerned. Obviously some analysis of this type is required before the payment of transfers or subsidies is even considered, and information in this regard would have to be provided by the recipient industry in terms of its plans for expansion and production. The effect of increased production by the industry concerned on the activities of other industries may be examined by the use of the input-output matrix. General effects on the income of the economy may be

analyzed through the application of an overall investment multiplier.

The effects of federal conditional grants to other levels of government could be determined in the same manner in which the effects of direct federal expenditures for similar purposes are analyzed. It is difficult, however, to determine the impact on the economy of unconditional grants. The nature of these grants is such that no indication is given of the use to which they are to be put. A special study of this area of expenditure would be required if we are to have an indication of the utilization of such funds by other levels of government.

Program Effects

The evaluation of program effects requires data which are not directly related to that required for the analysis of spending effects. It requires quantitative measurement or assessment primarily of the effect of government activities and projects on future production and employment. One of the difficulties of measuring the effects is the fact that they do occur in the future. Their estimation consequently involves a large element of uncertainty. Appropriate analysis for the evaluation of program effects, however, could take the form of an extension of cost-benefit analysis to include the repercussion effects which stem from or are induced by the existence of the government project. Despite the conceptual and statistical limitations of cost-benefit analysis, serious attempts have been made to employ it in the evaluation of various types of government projects in Canada as well as in the United States.¹⁵

¹⁵It is not intended here to delve into the details of cost-

Consider, in general, the program effects of an irrigation project. The government constructs a dam to provide water storage for irrigation. The effects of the existence of the created reservoir on income, production, and employment may be divided into the following categories:

Primary Effects

(1) Agricultural production and employment —

- (i) increased productivity of farm land currently under cultivation,
- (ii) production of land brought under cultivation as a result of irrigation,
- (iii) increase in the level of employment in the agriculture industry as a result of the increase in agricultural activity,

Secondary and Induced Effects

(1) Processing and marketing —

- (i) establishment of new processing plants for agricultural products or expansion of existing plants,
- (ii) increase in employment in the processing plants,
- (iii) increase in transportation and marketing activity,

(2) Induced activity in enterprises supplying consumer goods and services and capital goods to local farmers and people engaged in processing —

benefit analysis, its application, and its limitations. For literature on the subject of cost-benefit analyses, see for example, Supra, p. 12n and p. 92n.

- (i) increase in sales of existing enterprises,
- (ii) establishment of new enterprises to meet the demand for goods and services.

In the United States the Bureau of Reclamation has developed various means of measuring effects or benefits of this nature. The increase in farm production is measured by estimating the increase in the annual gross value of each crop produced.¹⁶ Secondary effects, such as the increase in processing, transportation, and marketing activities, are estimated in terms of percentages of gross value of the various crops produced. These percentages are based on studies of the processing and transporting conducted in relation to crop value. Similarly the expansion in local sales of goods and services to farmers is estimated by multiplying the estimated direct benefits accruing to farmers from the project by a percentage figure calculated on the basis of similar past projects.¹⁷

It was mentioned earlier that the difficulty of evaluating program effects may be lessened by establishing a more effective approach to program determination. Such an approach is provided through the program budget which features the identification and meaningful

¹⁶ R. N. McKean points out that estimates are made of anticipated crop patterns, yields, prices, etc. The crop yields "represent average yields under good farming practice. They are based on past production records and estimates made by individual farmers in the area" See R. N. McKean, Efficiency In Government Through Systems Analysis (New York: Wiley & Sons, 1958), p. 219.

¹⁷ For an account and appraisal of the methodology used by the Bureau of Reclamation in measuring direct and indirect benefits and for illustrations of its application to various irrigation projects in the United States, see Otto Eckstein, Water-Resource Development: The Economics of Project Evaluation (Cambridge: Harvard University Press, 1961), pp. 192 - 236; McKean, op. cit., pp. 185 - 244; and Julius Margolis, "Secondary Benefits, External Economies, and the Justification of Public Investment," Review of Economics and Statistics, XXXIX (August, 1957),

description of end-products and quantitative measurement whenever feasible, and places emphasis on systematic planning. The program budget also facilitates the application of cost-benefit analysis.

Economic growth may be slow as a result of inadequate capital formation or because resources, capital included, are not productive enough. With regard to the effects on future production or economic development, government projects of a capital nature have direct effects in the sense of adding to the stock of capital in a country and consequently to productive capacity. Governments construct capacity that leads to direct production. To the extent that such expenditures provide external economies to private industry they may lead to increased capital formation and productive capacity in the private sector. The government may also provide subsidies for private capital formation.

Government expenditures may also result in increased productivity. These are expenditures directed towards providing education, improving skills of workers, and advancing scientific and technical knowledge. It appears reasonable to assume that expenditures on research and education, particularly if continued over an extended period of time, will result in appreciable increases in technology and productivity.¹⁸ From the point of view of program effects the presentation of expenditures in terms of programs and objectives would serve to identify productivity-increasing expenditures (i.e. research in the field of atomic energy, agriculture research aimed at improving agricultural production, etc.) as well as capacity-creating

¹⁸ Attempts have been made to measure quantitatively the contribution

expenditures.

C. Other Considerations

A framework establishing a quantitative approach to the problem of expenditure evaluation is insufficient in itself for purposes of fiscal policy. Administrative procedures are important in expenditure determination, evaluation, and implementation. Furthermore, data concerning the government sector will not be of great value in determining the impact on the economy as a whole or in determining the need for fiscal action if information regarding activity in the other sectors of the economy is inadequate.

Role of the Treasury Board and the Department of Finance

The evaluation of the impact on the economy of government programs and projects in terms of long-run program effects and direct spending effects should be undertaken by both the Treasury Board Secretariat and the Financial Affairs and Economic Analysis Division of the Department of Finance working in close liaison. In the past there has been very little or no liaison between these two organizations. With regard to program effects, the Financial Affairs and Economic Analysis Division should be responsible for analyzing departmental long-range plans and proposed programs in the light of the conditions of the economy and from the point of view of their impact on economic growth. If the government has decided to pursue an active fiscal policy to help achieve a high level of economic growth, the Financial Affairs and

made to growth by education and advances in knowledge. See, G. F. Denison, The Sources of Economic Growth in the United States (New York: Committee for Economic Development, 1962).

Economics Division could be made responsible for recommending programs and projects whose long-term effects will contribute to economic growth. Depending on the degree of priority given to growth considerations by the government, the Treasury Board would be required to give them a certain weight in the annual estimates review process.

In respect to long-term considerations, the planning of programs on a five to ten year basis would provide the Financial Affairs and Economics Division with an opportunity to plan for economic growth. Only a small percentage of the total expenditures are controllable on an annual basis, but controllability is greatly enhanced on a five to ten year basis. An examination of long-term departmental expenditure programs would indicate the direction of expenditures and what implications they have in regard to economic growth, and whether growth could not perhaps be facilitated by re-directing these expenditures. With the Canadian Economic Council presently outlining goals for the economy, expenditure programs could be examined from the point of view of their contribution to the attainment of these goals, with consideration given to establishing priorities among programs in regard to these objectives and, in addition, perhaps recommending an entirely new field of government expenditure programs which would contribute to their attainment.

In addition to a review of expenditure programs from the point of view of the long-term program effects, a review is also required from the standpoint of the more short-term spending effects. An analysis of the immediate direct spending effects of individual programs could be conducted by the Treasury Board during its expenditure review. Weight could be given to the programs and projects which have the effects that have been determined desirable by the Financial

Affairs and Economics Division in the light of prevailing or anticipated economic conditions. For example, if it has been determined that certain industrial activity in a designated area requires the stimulation that direct government spending might provide, it would be the responsibility of Treasury Board, in its decisions regarding priorities among programs and projects, to take this into consideration and give additional weight to those programs and projects in which the direct spending effects are primarily directed to the specified industry in the designated area.

The Program-Economic Budget and Parliament

At present, consideration of the expenditure estimates in the House of Commons is on a fairly general basis with attention primarily focussed on policy. The House, sitting as the Committee of Supply, has neither the time nor the means of conducting a thorough review of detailed expenditures. Such a review is best reserved for a revived Standing Committee on Estimates. The Committee of Supply would continue its general review except that under the program budget a greater amount of information in respect to questions of "what" and "why" concerning government expenditures would be presented. It would provide the basis for a more objective examination of government operations and would enable members of Parliament to relate departmental operations to government policy. While appropriations would continue to be made on an annual basis, the inclusion of detailed expenditures for future years would provide members of Parliament with a view of the commitments current appropriations involve for the future and would illustrate in quantitative terms the direction in which departments are heading.

It is proposed that annual Parliamentary appropriations be made on the basis of programs, that is, one appropriation or vote for each program. In this way all related operations, whether they are of a current or capital nature, which form one program would be considered by the Committee of Supply prior to the appropriation. It is also proposed that allotments be made on the basis of activities. The allotment of funds on this basis would allow departments to administer their operations without the niggling control presently exercised over departmental administration by the Treasury Board. Treasury Board approval would be required only if a department wished to transfer funds from one activity to another. The department would, however, be held accountable for the manner in which funds are administered and could be required to submit periodic reports to the Treasury Board regarding progress and accomplishment. Such reports would be taken into consideration by the Treasury Board secretariat in its continuing review of departmental programs and in the annual estimates review process.

Information regarding the impact of government expenditures on the economy could be tabled in Parliament as a supplement to the annual estimates blue book showing the spending effects in the aggregate and for the individual programs, and indicating anticipated program effects. Such a supplementary tabulation could include statements of fiscal policy and the goals that the government is striving to achieve in this regard. Special attention could be given to new policies that the government is introducing in an attempt to attain stated goals. It is submitted that such factual data on government operations would open the way to a more objective review of fiscal policies and of the contribution

made to fiscal objectives by expenditures in general.

Other Fiscal Considerations

Among the criticisms levelled earlier at the present budgetary system as a tool of fiscal policy were its lack of comprehensiveness and lack of flexibility. With regard to the former the scheme proposed in this study has been designed to cover all government expenditure transactions including those presently considered as non-budgetary and the transactions of Crown Corporations. It has been suggested that Crown Corporations prepare their budgets on a program basis to be submitted to the appropriate Cabinet minister and to Treasury Board and Parliament. As in the case of departmental expenditures, this would permit a review to be conducted at these levels of the plans of the Corporations and the direction in which their operations are moving. This does not imply that the Corporation budgets necessarily be subjected to the type of Treasury Board approval and Parliamentary authorization process characteristic of departmental expenditures. The purpose of Treasury Board and Parliamentary review would be to consider the policies associated with Corporation operations, to co-ordinate departmental and Crown Corporation operations, and to analyze the effects which the operations of the Corporations are likely to have on the economy. With respect to the economic impact it would be necessary to classify the expenditures of Corporations on the basis of their economic character in the manner that is proposed for departmental expenditures. The result would be a uniform framework in which total government expenditures could be analyzed.

Medium and long-term flexibility of expenditures is inherent in the program budget in the sense that expenditure plans and programs are subject to continual review. Short-run flexibility will likewise be facilitated through the program scheme as a result of the process of planning and establishing priorities. Those projects which have been determined to be of lesser priority within programs and between programs could be maintained in the overall master plan of a department and could be implemented should economic conditions warrant. In this regard they would derive their justification not only from the fiscal point of view but also from the point of view of the program of which they are a part, and which has already been established as desirable or necessary on social and economic grounds. Projects currently under construction would also be more flexible in the sense that their rate of implementation may be altered. Certain projects which have been planned to be undertaken over a two or three year period and for which estimates of requirements have already been made could be accelerated or the current year expenditures could be postponed until the following years.¹⁹ Formal plans of such projects, which include information on direct material and manpower requirements as well as indirect income and economic activity generating capacity, would indicate which of the projects should be altered in light of prevailing or anticipated conditions in the economy.

The Possibility of a System of Regional Accounts

In recent years in the United States, in the government and in

¹⁹Steps have recently been taken in this direction in the Department of Transport. See Appendix D, p. 210.

academic circles, considerable attention has been focussed on the possibility of developing a system of regional accounts and their usefulness for public and private decision-making.²⁰ A system of regional accounts would not only serve to help local public officials analyze the effects of their policies on the region, but would assist in the evaluation of the regional impact of national policies and activities. Or as W. Z. Hirsch has stated, "a workable system of regional accounts could help provide an informational base on which federal and state policy-makers could make better decisions consistent with both local and national interests."²¹ Such a system would be of considerable importance in examining depressed and disorganized areas which seem to exist even when the overall economy is experiencing prosperity.

One aspect concerning the construction of a system of regional accounts which has been subject to a certain degree of controversy is the question of whether it is feasible to disaggregate the national accounts to a regional basis. The significance of such a disaggregation is not disputed, for it would permit comparability between regions by ensuring that the statistical data are uniform and would enable an examination

²⁰See Werner Hochwald (ed.), Design of Regional Accounts, Papers presented at the Conference on Regional Accounts, 1960 (Baltimore: John Hopkins Press, 1961); Werner Z. Hirsch (ed.), Elements of Regional Accounts, Papers presented at the Conference on Regional Accounts 1962 (Baltimore: John Hopkins Press, 1964); and Richard Ruggles and Nancy Ruggles, "Some Relationships Between National Accounts and Regional Accounts," Proceedings, American Statistical Association, 1959.

²¹Hochwald, op. cit., Preface viii.

to be conducted of the impact on the different regions of something taking place in the nation as a whole. It is the opinion of Richard and Nancy Ruggles that disaggregation in the present system of national accounting is not feasible because "there are too many places in the national accounts where the introduction of a regional breakdown is not feasible due to the procedures by which the national estimates are made."²² What would be required for the establishment of a system of regional accounts on a national level are new statistical sources and new techniques of gathering statistical data.

On the matter of regional accounts, H. S. Perloff has submitted that;

The most hopeful possibility at the present point in time . . . is to build a system of regional accounts centering on a geographical breakdown of the national interindustry sales and purchases estimates. . . . the purchases-sales estimates will be integrated . . . with the national income and product accounts, so that much of the key data will be available on an industry basis.²³

He submits that information which is lacking in the inter-industry accounts, such as man-power data, could be provided by an extension of these accounts and by supplementary tables.²⁴

Despite the differences of opinion that have appeared regarding the method of constructing a system of regional accounts, there is general agreement that such a system would be highly useful. In relation to the proposed program-economic budget such a system would particularly be of significance in analyzing general government programs which are

²²Ibid., p. 140.

²³Ibid., p. 62.

²⁴Ibid., pp. 63 - 64.

not designated to any specific areas. Even in the case where a program or project is undertaken in a specified geographical area, a detailed system of regional accounts would indicate interregional relationships and consequently the net effect of the program on the particular area.

Implications In A National Economic Budget Setting

A national economic budget is composed of comprehensive statistical data regarding the transactions of the entire economy. It is directed mainly to a searching analysis of existing economic conditions and the estimation of future development patterns to indicate to the government and the private sector the most advantageous directions for development. It can indicate the conflicting demands on the economy, locate bottlenecks or imbalances, and give some indication as to how these bottlenecks may be removed. In general, a national budget would be of great value in assisting the government to pursue appropriate fiscal and financial policies.

A national economic budget consists, first of all, of an estimate of the level of gross national product and its components for the coming fiscal year and for a given future period. These global estimates are then translated into detail to include an estimate of the expenditure on different commodities and services, the amount of these commodities produced domestically, and the amount imported and exported. In this manner any surpluses or shortages may be determined. Such a budget also includes an analysis of the factors of production and distinguishes industrial sectors and geographical regions. Estimates of the demand for, and supply of various productive resources serve to locate shortages and surpluses. Other details generally follow, such as data on industries

which appear to be in disequilibrium and on resources which appear to be in short supply. The result is a comprehensive analysis of demand and supply, input and output, and employment and unemployment in each industry and region of the economy. With the location and isolation of bottlenecks and imbalances, appropriate policies which would help redress these imbalances could be introduced.²⁵ The result would be more effective use of government policies and programs to maintain a balanced and growing economy.

The proposed program-economic budget outlined earlier could readily be integrated into such a national economic budget, assuming uniformity of accounting concepts and techniques. The economic character classification would show the types of commodities and services purchased by the public sector and the resources used. Given an imbalance or gap in any industrial sector of the economy, programs could be introduced which are designed specifically to fill such a gap. At the same time the programming of expenditures would indicate the contribution being made by the government towards providing for social wants or redistributing income.

²⁵ For a more detailed account of national economic budgeting, see W. Arthur Lewis, The Principles of Economic Planning (Washington: Public Affairs Press, 1951) and W. H. Beveridge, Full Employment In A Free Society (New York: Norton and Company Inc., 1945). For an illustration of econometric techniques and models of a nation's economy and an analysis of economic policies in such a framework, see Jan Tinbergen, On the Theory of Economic Policy; Centralization and Decentralization in Economic Policy; and Economic Policy: Principles and Design (Amsterdam: North-Holland Publishing Co., 1952, 1954 and 1956 respectively); H. Theil, "On the Theory of Economic Policy", American Economic Review, XLVI (May, 1956), pp. 360 - 66; and C. J. Van Eijk and J. Sandee "Quantitative Determination of an Optimum Economic Policy," Econometrica, LXVII (Jan., 1959), p. 1 - 13.

While a national economic budget appears to be practically a prerequisite for effective use of fiscal policy, among the major obstacles to its present introduction is the lack of adequate factual information on the operations of the economy and the difficulties of making forecasts of economic activity. The development of a national economic budget requires greatly improved economic statistical data and processing methods. It requires the preparation of figures of total unemployment, of unemployment by sectors and by regions in the economy, and data showing employment and unemployment by major industrial groups and by categories of workers. It also requires the regular collection and interpretation of a wide range of statistical data relating to the economic activity in each branch or area of the national economy. Furthermore, it requires projections which will serve as a guide for introducing programs which would assist in moving the economy forward consistently. Long-range needs for balanced economic expansion and high levels of employment must be estimated to which fiscal programs may be geared. Improved forecasting techniques are required, however, before this can be realized.

The Experience of Sweden in Planning

and National Accounting

Sweden is one of the countries which has pioneered in the post-war period in attempts to develop national economic budgets and introduce effective fiscal measures, both on the revenue and expenditure side, for the promotion of economic stability and balanced growth. At the beginning of each year an annual national budget is prepared and the government's fiscal budget is shaped taking into consideration the

information contained in the national budget regarding the state of the economy.

The development of the national budget in Sweden²⁶ dates back to the depressed 1930s when the demand for general economic information led to the foundation of the National Institute of Economic Research. This institute was assigned the task of surveying and analyzing economic developments. The resulting information was then taken into consideration when the state budget was being formulated. A formal national budget, however, was not prepared until 1948 when a National Budget Delegation was established. It was assigned the responsibility of conducting economic surveys and became a forum for discussion of future economic development. At present this function is performed by the Research Council which replaced the Delegation.²⁷

²⁶For a detailed account of national budgeting and planning in Sweden, see Ingvar Ohlsson, "The Swedish National Budget", Skandinaviska Banken Quarterly Review, Vol. 38, 1957 (Stockholm, Sweden), Gösta Rehn, "The National Budget And Economic Policy", Skandinaviska Banken Quarterly Review, Vol. 43, No. 2, 1962, and Ingvar Svennilson and Rune Beckman, "Long-Term Planning in Sweden", Skandinaviska Banken Quarterly Review Vol. 43, No. 3, 1962.

²⁷The National Budget Delegation was set up as an institution for the development and study of statistics on private and public plans, foreign trade, consumption, production and production costs, the effect of government economic policy on employment, etc. In 1957 the secretariat of the Delegation was converted into the Economic Division of the Ministry of Finance. The successor to the Delegation, the Research Council, now functions as adviser and examiner of the Division's work. This Council is composed of representatives from important research organizations of the business sector and the labour organizations, together with representatives from the Institute of Economic Research. See Ibid.

The present practice in Sweden is to draw up a preliminary national budget at the beginning of the year followed by a revised national budget a few months later based on more up-to-date material. The budget consists of estimates of the general economic developments in the coming year. It shows quantitatively the balance of resources in the economy, that is, the total supply of goods and services and the use of these for different purposes.

Sweden has also engaged in long-term planning (five-year plans) through Commissions created for this purpose. These Planning Commissions are composed of civil servants, representatives from trade unions and employers' organizations, and economists from the academic field. The Commissions suggest general targets for long-term national development and indicate the types of policies that would induce economic units to attain these targets. Hence, they are not plans in the strict sense but are of a less precise character and are subject to revision from year to year. Furthermore, targets and trends are indicated only for national aggregates or for broad industrial sectors. Nevertheless, by the collection of material on sector trends, perspectives and plans, by the co-ordination of them, and by the rolling adjustment of plans, the Planning Commissions and their permanent secretariat provide continuous information and advice for the long-term budgetary policy of the government. The government now prepares long-term government budgets as a supplement to the annual budgets.

Sweden has given considerable attention to fiscal policy since the 1930s. Through the budget reform of 1937 the principle of the one year balance of the budget was abandoned, and it was instead declared

sufficient that the budget be balanced over a period of years. Real economic factors, such as total employment, growth, and price stability, have been given priority over matters such as the government's asset-liabilities position.²⁸ A further budgetary reform in 1947 saw the introduction of emergency or special budgets which are annually voted by the legislature but are only implemented when the state of the economy warrants their implementation.²⁹ These budgets generally consist of appropriations for projects of a capital nature and amount to approximately 6 percent of total fixed investment. In this way an emergency program of investment projects that could be started quickly is kept up to date.

In general, the attitude prevailing in Sweden regarding anti-cyclical policy and the possession of a battery of advanced economic instruments³⁰ have in recent years given that country a smoother rate of economic growth.

²⁸For an account of the 1937 budgetary reform in Sweden, see "That Wonderful Swedish Budget," Fortune, September 1938.

²⁹For a brief account of Sweden's emergency budgets, see Jesse Burkhead, Government Budgeting (New York: John Wiley & Sons, Inc. 1956) p. 198.

³⁰Among these instruments not already mentioned are anti-cyclical investment funds, housing and agriculture policies, and stress on labour retraining and mobility.

VI

THE PROGRAM-ECONOMIC BUDGET AND THE ATTITUDE OF THE CANADIAN GOVERNMENT

The Glassco Commission, in its report on government organization and procedures, made various recommendations regarding financial organization and management. Following the report the government created a Bureau on Government Organization within the office of the Privy Council to review the Commission's report and to select those recommendations for government approval that it determined were readily applicable and desirable. Of the twenty-seven recommendations made by the Commission on financial management more than half have been approved in principle.¹ Among these are the recommendations that departmental expenditure estimates be prepared on the basis of programs of activity and that more objective standards for expenditure analysis be developed and employed by senior departmental officials and by Treasury Board in the expenditure review process.²

Treasury Board Attitude

The Bureau on Government Organization has been transferred to become a part of the Treasury Board secretariat. The responsibility for

¹The Senate Of Canada, Proceedings Of The Standing Committee On Finance, To whom was referred the Estimates for the fiscal year ending March 31, 1965. October 13, 1964, p. 145.

²Canada, The Royal Commission On Government Organization (Ottawa: Queen's Printer, 1962), Vol. I, p. 100.

analyzing the Glassco Commission's recommendations and taking the necessary steps to implement them now rests with the Treasury Board and its secretariat. In the past the Treasury Board has made various changes in the form of estimates presentation, but the work towards adopting the Glassco Commission's views on reform of the estimates is proceeding rather slowly, in typical civil service fashion. Among other recommendations of the Commission which are under consideration are those pertaining to the decentralization of financial control in the sense of placing greater responsibility in the hands of the individual departments, the future role of the Treasury Board and the Comptroller of the Treasury, reporting techniques, and accounting and auditing procedures.

To determine the desirability and practicality of these recommendations, especially those associated with decentralized control, the Treasury Board secretariat, on the authorization of the Board to explore these questions, initiated four financial management studies in four separate government departments, namely, Northern Affairs and National Resources, Transport, Agriculture, and Veterans Affairs.³ The services of four outside management consulting firms were engaged for the purpose of conducting these studies. The separate studies were fairly unanimous in approving the Glassco recommendations. This is not surprising for the Commission itself had conducted an intensive study of these matters, and had drawn upon management consultants in doing so.

³Proceedings, op. cit., p. 147.

It now remains for these recommendations to be implemented. It is the opinion of one Program Analysis Director in the Treasury Board secretariat that it will take up to five years to complete total implementation of these recommendations.

Even while the Glassco Commission was in the process of conducting its examination, and while its proposals were under initial review, the Treasury Board secretariat began to give serious consideration to such aspects of financial administration as the preparation and use of performance measurement, and initiated a series of work study seminars among its staff and participated in work study conferences. There was general agreement on the usefulness of such measurement in promoting efficiency in government operations and also in assisting treasury officers during the establishment review. The Treasury Board secretariat also gave serious consideration to the desirability of preparing expenditure estimates on the basis of programs and activities when it established the present requirement that departments submit two year forecasts of their expenditures along with their annual estimates.

The adaptation of the budget for fiscal policy analysis and implementation by the construction of budgetary economic accounts can be considered to be in the very initial stage of development. Consideration has been given from time to time to the need for improvements in the budget presentation to facilitate an analysis of its impact on the economy, but no well defined plans for proceeding in this direction have been established. Understandably the Dominion Bureau of Statistics and the Financial Affairs and Economic Analysis Division of the Department of Finance are very interested in developing some classification

scheme which would allow government activities to be evaluated in the framework of the operations of the national economy, but the establishment of such a scheme requires the co-operation of the departments and the Treasury Board.

Attitude in Other Government Circles

There has been a general acceptance of the recommendations of the Glassco Commission regarding financial administration throughout the government organization. It has already been mentioned that many of these recommendations have been approved in principle by the Cabinet. Various government departments have been co-operative in attempts to determine the desirability and practicality of the proposals.⁴ Having determined that they are desirable, the Treasury Board and several departments have arranged to proceed with their implementation. First and foremost has been the reform of expenditure estimates on the basis of programs of activity and the establishment of performance standards.

The Department of Northern Affairs and National Resources has been the leading department in establishing program budgeting and hopes to have it completely implemented within approximately two years. The Department of Transport has also made advances in planning and defining the objectives of its operations. For example, the Air Services Division of the Department has recently instituted the process of planning on a five year basis. These are formal planning documents on the basis of the present administrative,

⁴Ibid., p. 147.

operational, and capital vote structure and on the basis of the department's regional organization. Staff and equipment requirements and proposed construction and maintenance works are outlined for each fiscal year for a five year period.⁵

The Senate Standing Committee on Finance has also recently given formal approval to certain recommendations of the Glassco Commission regarding the form and review of estimates. It approved, with some reservation, the proposal that departmental estimates be prepared on the basis of programs of activity.⁶ The Committee also agreed that the preparation by departments of long-term plans of expenditure requirements by programs would be highly useful.

Political Considerations and the Attitude of Parliament

While the establishment of the proposed program-economic scheme in the federal government appears feasible, it is conceivable that various aspects of the political process may limit its practical value and use.⁷ The use of quantitative analysis for evaluating government expenditure programs, whether in respect to resource allocation or fiscal policy, would appear to be in conflict with certain characteristics of the political process, such as political expediency. It is not inconceivable that the government may propose activities or projects to obtain the support of certain areas or groups in the country, though the priority of such projects may be difficult to justify on social and

⁵See Appendix D, pp.210-212.

⁶The Senate Committee was of the opinion that standard objects of expenditure were "relevant details" and should not be excluded from the estimates. See The Senate of Canada, Proceedings, Report of the Committee Nov. 25, 1964, p. 314.

⁷For an interesting discussion of the political process in

economic grounds. Individual members of Parliament may also press for various activities or projects to be undertaken in their constituencies. Members are after all popularly elected and must consider the views and interest of their constituents. It is consequently understandable that members will exert pressure on Cabinet ministers to introduce various expenditure projects in their constituencies, even though such projects may be quite low on the priority scale, and scrutinize expenditure estimates with their ridings in mind. It is sometimes implied that individual members care little for the actual form in which the Estimates are submitted, or how much is spent on programs or activities or objects, or for objectively examining expenditures from the point of view of efficiency in resource allocation or administrative efficiency. Their concern is what portion of the expenditures of departments affect their ridings. It is also sometimes suggested that members of Parliament in opposition are not often concerned with an expenditure for its own sake during the estimates review but may move for a reduction in expenditures to present a motion of want of confidence in the government. It would be desirable to dispense with this ruling. Parliament cannot exercise expenditure control if it is unable to reject an expenditure without precipitating a general election.

The question arises concerning the value of developing objective criteria for evaluating expenditure proposals and establishing priorities when there is a strong political element present in the decision-making process. The political element in the determination and review process

budgeting in the United States, see A. Wildavsky, The Politics of the Budgetary Process (Boston: Little, Brown and Co., 1964).

by the executive and legislature will no doubt always be present. Departmental administrators, however, in their function of planning and evaluating programs and projects, should base their recommendations and decisions to the greatest extent feasible on quantitative approaches and should attempt to systematize this process. If their decisions with respect to a proposed project are reversed by the government or their recommendations go unheeded due to political pressures and considerations then the departmental officials must accept this. As far as they are concerned they will have fulfilled their function in such matters, that is, they have presented factual data, which politicians may use or disregard. In the past certain capital projects have been rejected following departmental appraisal even though there was considerable pressure for these projects. In such cases it was found that the benefits did not justify the costs or that there was no urgency for these projects.

With regard to fiscal policy and politics it was pointed out in an earlier chapter that certain difficulties arise in implementing fiscal policy due to political pressures. The government may often use the budget for political gain while the parties in opposition generally attack budgetary deficits and surpluses in an attempt to embarrass the government. It is hoped that the presentation of well defined fiscal goals and statistical data concerning the economic impact of government expenditures will provide the framework and the type of information which would cause members of Parliament to adopt a more objective attitude towards fiscal policy. It may serve to give members and the public a better understanding of fiscal policy and its aims and effects.

In respect to the type of information that would be made

available to Parliament as a result of the implementation of the program-economic budget, there are conflicting views among members of Parliament. One prominent Parliamentarian expressed the opinion during a personal interview that members of Parliament in general would favour the program budget and more information regarding expenditure objectives. He stated that information on the impact of federal government expenditures on the economy, if tabled as a supplement to the Estimates Blue Book, would be very useful and that he would like to see a system of National Economic Budgeting in which the effect of provincial and municipal expenditure as well as federal expenditure would be indicated. Another Parliamentarian was less optimistic about the value of a detailed expenditure presentation. While he favoured quantitative information regarding the impact of expenditures on the economy presented in a straight-forward and simple form, he believed that a voluminous and detailed expenditure presentation would be confusing and would be an invitation to time-consuming and unproductive haggling during legislative review. He suggested that excessive budgetary detail could conceivably result in a failure of members to study the material provided.

The judgement underlying this thesis is that if the government is to seriously pursue an active fiscal policy and aim for efficiency in the allocation of resources, factual information should be taken into account in the decision-making process. Regardless of the level at which decisions are made there can be little argument that a more rational choice is made by the decision-maker when he is in full possession of the relevant facts than otherwise. For instance, there is no doubt that factual information on government operations would pave the way to a more

objective review by Parliament and more constructive criticism by opposition members. The acceptance of the proposed approach to expenditure analysis and decision-making, however, must be fairly complete if it is to be effective. There is considerable evidence that the principles are acceptable to departmental administrators. The primary question is the extent to which politicians are prepared to accept the concept of decision-making on the basis of factual data and objective criteria and the extent to which objective analysis is likely to replace political considerations in the decision-making process. It is difficult to arrive at any firm conclusion in this regard. At the present time it can only be assumed that factual information or objective criteria, even though they may not be perfect, when presented to politicians cannot be completely ignored by them for the sake of political expediency but will have some bearing on their decisions.

VII

CONCLUSIONS

In general, there is no question that government expenditures do influence economic activity. The nature and extent of this influence, however, is difficult to assess. An analysis of expenditures from the standpoint of their effect on income, production, employment, and prices necessitates information or data regarding the composition of government purchases and other various payments and their allocation between industries, groups, and geographical regions of the economy. In Canada, in view of the magnitude of government expenditures and considerations of fiscal policy, the interrelations between private and public transactions warrant closer attention than they have received in the past.

The application of fiscal policy points toward the need for a framework within which an analysis of the impact of government expenditures may be conducted. Such an analysis is desirable not only for those government activities which constitute fiscal policy, but also for activities which are undertaken for purposes of securing adjustments in the allocation of resources and the distribution of income. An indication of the impact on the economy of the latter type of expenditure activities would, in the light of prevailing or anticipated economic conditions, facilitate the determination of whether additional government action is required to achieve established fiscal objectives

and the direction of such action. Furthermore, information regarding the economic impact of individual government activities would facilitate the reconciliation of fiscal policy objectives with the other major purposes of expenditure policy.

A review of the total federal expenditure relative to the Gross National Product and a review of the various functions undertaken by the federal government has indicated that there is a good deal of scope for fiscal policy in the area of federal expenditures. A review of post-war fiscal policy in Canada has indicated that many of the fiscal measures that have been introduced have been in this area. The government has concentrated on both expenditure measures and tax measures in its fiscal policies and at times has placed greater emphasis on expenditure policies.

An examination of the budgetary system in Canada reveals that little consideration is generally given to the impact of government expenditures on the economy in the annual expenditure determination and review process. Even in instances when the determination of the effects of certain government operations on the economy is attempted the required information is not available. A framework or scheme through which information or statistical data relevant to such an analysis could be obtained does not exist. The result is that it is virtually impossible to assess the impact of government operations on the economy or to determine the effect of specific measures introduced as fiscal policy.

The effects of government expenditure on the economy may take the form of spending effects or program effects. Spending effects, which are concerned with the immediate or short-term effects on income,

production, employment, and prices resulting from government purchases and transfer payments, are of particular significance in respect to current economic activity and aggregate demand. Changes in economic activity may be caused by changes in the size and composition of government demand for goods and services and changes in transfer payments. In regard to program effects, the existence of the asset which is created by a government expenditure program may stimulate economic growth and development. Development in various regions may be induced through the external economies provided by such government created assets as roads, hydroelectric plants, etc.

An analysis of the spending and program effects of government expenditure necessitates careful consideration of the relation of proposed government expenditures to the functioning of the economy as a whole. An expenditure pertaining to one group, industry, or region may have certain effects on the rest of the economy. Information concerning the composition and distribution of public expenditures and their relation to the various economic units in the economy is required for purposes of assessing these effects. It is submitted that a program-economic classification framework would provide the basis for obtaining this type of information.

The expenditure classification scheme characteristic of the program budget and various procedures inherent in this type of budgeting, such as planning and quantitative systematic analysis, are established as prerequisites in the development of a scheme for analyzing spending and program effects and implementing fiscal policy. The presentation of expenditures on the basis of programs would indicate the nature and

purpose of the expenditures. Following the development of the program classification it is proposed that an economic character classification of expenditures be applied to the program classification scheme. The economic classification, designed on the basis of the national accounts, would provide information for the purpose of viewing the role of federal expenditures within the context of the economy as a whole. It would provide information relevant to the analysis of the impact on the economy of each individual program and activity as well as to the analysis of the expenditures in the aggregate.

It has been emphasized that an analysis of the impact of government expenditures on the various industrial sectors of the economy would be greatly enhanced by the development and utilization of inter-industry flow data. It is not enough to consider only direct government purchases of manpower and materials. The manpower and materials which are utilized by the various industries involved in the production process of the goods and services purchased by government must also be considered. This chain of effects cannot be determined without regard to inter-industry relationships. It has been submitted that the proposed detailed economic character classification scheme would provide the type of information concerning government purchases that is required for the compilation of inter-industry tables to be used in analyzing economic effects.

The effectiveness of expenditure policy to counter short-run economic fluctuations resulting in unemployment or inflation depends to a considerable extent on the flexibility of the budget in the implementation of expenditure programs and projects in response to short-run

changes in economic activity. To the extent that flexibility is increased by having projects of lesser priority, within an approved program, planned and constantly ready for implementation, and by providing for the possibility of altering the rate of implementation of programs and projects already in progress, the degree of flexibility will be increased with regard to the expenditure side of the budget. Furthermore, an analysis of the effects of the various programs and projects would facilitate decision-making in respect to altering or implementing those programs and projects which would have the desired effects on the economy. This in turn depends on the ability of the government to determine the needs of the economy. The preparation of a national economic budget indicating imbalances and bottlenecks in the economy would be of considerable value in reaching decisions in respect to the need for fiscal policy.

In regard to economic growth, with targets presently being established for the economy by the Economic Council of Canada, the long-range planning of government programs and the determination of the long-term effects of the programs is desirable. If the proposed scheme is adopted, an assessment of the impact that expenditure programs are likely to have on the economy in terms of contributing towards the attainment of these targets would be facilitated. The scheme would also provide the framework in which policies and programs may be introduced for the specific purpose of achieving these targets.

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APPENDIX A

PUBLIC ACCOUNTS AND NATIONAL ACCOUNTS RECONCILIATION — FEDERAL GOVERNMENT REVENUES AND EXPENDITURES

The reconciliation between the Public Accounts and the National Accounts consists of the adjustment of the conventional budgetary data of government revenue and expenditure to conform to the basic definitions incorporated in the National Accounts. In this adjustment government budgetary data are placed on a calendar year basis, non-budgetary transactions such as those relating to the Old Age Security Fund, government superannuation funds, etc. are included, government loans are excluded, purely bookkeeping transactions such as the purchase and sale of existing capital assets are excluded, and corporation taxes are adjusted to an accrual basis.¹

This process of Public Accounts and National Accounts reconciliation is described in the Budget White Papers as follows:

The National Accounts budgetary presentation differs from the parliamentary presentation in several ways. Only income and expenditure transactions which have a direct and immediate impact on the flow of incomes in the economy are included in the National Accounts budgetary presentation; financial transactions (i.e. loans), which result in changes in the liabilities of one sector of the economy to another, are excluded from the National Accounts presentation. A number of bookkeeping items in the parliamentary accounts of purely internal significance and having no impact on the private sector are also excluded from the National Accounts presentation.

A number of items which are excluded from the parliamentary budgetary accounts are of immediate significance to the private incomes stream. The National Accounts embrace these items, the most important of which are payments into and out of the Old Age Security Fund, the Unemployment Insurance Fund, and the government pension funds, by those contributing or drawing benefits.

National Accounts items are entered as they accrue, that is, at the time when the economic impact is felt on the economy, since this is the basic method used in business. Corporation income taxes in particular require a major adjustment from the public accounts to a National Accounts basis. These taxes will have been paid on an instalment basis beginning eight months before the end of the companies' fiscal year and ending four months after. Corporations can elect to estimate current income on the basis of last year's income or on the basis of their current records, but

¹ See Dominion Bureau of Statistics, National Accounts Income And Expenditure, 1926 - 1956, (Ottawa: Queen's Printer, 1962), p. 129.

must complete the current year's payment within four months of the end of that year. As a result, corporations may accrue tax liabilities a number of months before tax payments are actually made and recorded in the public accounts. Tax accruals are directly related to corporate profits at the time they occur, and profits move with the business cycle. Accordingly, the recording of tax accruals and the analysis of the government sector, on a National Accounts basis, may permit a more meaningful appreciation of the timing of changes in revenues of the government sector in relation to fluctuations in economic activity. Similarly, timing adjustments are made on the expenditure side of the National Accounts to put government purchases of goods and services on an accrual basis, rather than at the time actual payments are made.²

This reconciliation is illustrated in the adjoining table. In this table the government revenues and expenditures are shown for the government's fiscal year rather than the calendar year which is the basis of all data in the National Accounts. The government revenue and expenditure data are computed on the basis of the National Accounts in terms of quarter yearly periods, and the fiscal year 1964 - 65 illustrated in the table contains the National Accounts data for the last three quarters of the 1964 year and the first quarter of 1965.

² See House of Commons, Budget Papers presented by the Honourable Walter L. Gordon, M.P., Minister of Finance for the information of Parliament in connection with the Budget of 1965 - 66 (Ottawa: Queen's Printer, 1965), pp. 22 - 27.

FEDERAL GOVERNMENT REVENUES AND EXPENDITURES-PUBLICACCOUNTS AND NATIONAL ACCOUNTS RECONCILIATION1964 - 65

	\$ Million
<u>Revenue</u>	
1. Budgetary Revenue	7,136
2. Supplementary period adjustment ^a	-10
3. Extra-budgetary revenues	
Old Age Security tax collections	956
Prairie Farm Assistance Act Levy	10
Unemployment insurance employer-employee contributions	307
Government pension funds, employer- employee contributions	251
Interest receipts of social insurance and government pension funds	157
4. Corporate income tax ^b : excess (-) of accruals over collections	-137
5. Profits before taxes (net of losses) of government business enterprises	244
6. Interest on loans, advances and invest- ments	169
7. Less: Budgetary return on investments ..	-380
8. Less: Postal revenue	-230
9. Budgetary revenue items offset against budgetary expenditures	-112
10. All other adjustments to budgetary revenue ^c	<u>-48</u>
11. Total Revenue, National Accounts Basis ..	8,313

Expenditure

1. Budgetary expenditure	7,219
2. Supplementary period adjustment ^d	-6
3. Expenditures of extra-budgetary funds	
Old Age Security Fund payments	889
Unemployment Insurance benefits	332
Government pension fund payments ...	97
Prairie farm assistance payments ...	10
4. Transfers to extra-budgetary funds	-63
5. Adjustment to place other government funds and crown agencies on a disbursement basis ^e	-30
6. Budgetary expenditures offset against income of government business enterprises	
Post office expenditures	-211
Deficits of government business enterprises	-80
7. Capital assistance to non-defence industry ^f	-77
8. Reserves and write-offs	-42
9. Budgetary revenue items offset against budgetary expenditure ^g	-112
10. All other adjustments to budgetary expenditure	<u>55</u>
11. Total Expenditure, National Accounts Basis	7,981
Surplus (+) or deficit (-), National Accounts Basis	332

^aIn the National Accounts, revenues in the supplementary period are shifted to the following year.

^bTaxes on government business enterprises are excluded from this item and included in item 5.

^cThese adjustments are largely revenue items not relevant for the National Accounts such as proceeds from sales of existing assets.

^dIn the National Accounts, expenditures on goods and services in the supplementary period are split evenly between adjacent fiscal years. Other expenditure items are shifted entirely to the next fiscal year.

^eThis adjustment replaces budgetary appropriations to various funds and agencies by the outlays actually made by these funds and agencies.

^fGovernment capital assistance to industry appears as part of business gross capital formation and is removed from the government sector to avoid double counting in the National Accounts.

^gThe largest component of this item consists of revenue from sales of goods and services by the government sector. These sales appear as final expenditure of the private sector and are deducted to avoid double counting.

SOURCE: House of Commons, Budget Papers, 1965 - 66, pp. 25 - 26.

APPENDIX B

FEDERAL, PROVINCIAL AND MUNICIPAL GOVERNMENT EXPENDITURES

TABLE B - I

GOVERNMENT EXPENDITURE BY MAJOR ECONOMIC
CATEGORY ON NATIONAL ACCOUNTS BASIS^a
(In \$ million and as Percentage of
Gross National Product)

Economic Category and Level of Government	1950		1956		1963	
	Amount	Per Cent	Amount	Per Cent	Amount	Per Cent
Goods and Services	2,344	13.0	5,386	17.6	8,076	18.8
Federal	977	5.4	2,683	8.8	2,927	6.8
Provincial- Municipal	1,367	7.6	2,703	8.8	5,149	12.0
Transfer Payments and Subsidies	2,071	11.5	3,468	11.3	7,884	18.3
Federal	1,352	7.5	2,351	7.7	4,505	10.5
Provincial- Municipal	719	4.0	1,117	3.6	3,379	7.8
TOTAL	4,415	24.5	8,854	28.9	15,960	37.1
Gross National Product	18,006		30,585		43,007	

^a Includes intergovernmental transfers

SOURCE: Dominion Bureau of Statistics, National Accounts, Income and Expenditure 1926 - 56, 1961 and 1963.

TABLE B - II

NET EXPENDITURE OF ALL GOVERNMENTS BY FUNCTION

EXCLUDING INTERGOVERNMENTAL TRANSFERS, 1961-62

(\$ Million)

Function	Total Amount Expended				% of Amount Expended		
	Fed.	Prov.	Mun.	Total	Fed.	Prov.	Mun.
Defence Services and Mutual Aid	1,647	-	-	1,647	100.0	-	-
Veterans' Pensions and Other Benefits	337	-	-	337	100.0	-	-
Health, including hospital care	366	600	66	1,032	35.4	58.2	6.4
Social Welfare	1,424	275	42	1,741	81.8	15.8	2.4
Education	94	841	886	1,821	5.1	46.2	48.7
Transportation and Communications	430	659	346	1,435	30.0	45.9	24.1
Natural Resources and Primary Industries	403	202	-	605	66.7	33.3	-
Debt Changes	690	84	106	880	78.4	9.5	12.1
Contributions to Government Enterprises	171	5	18	194	88.0	2.6	9.4
General Government	287	135	150	572	50.2	23.6	26.2
Protection of Persons and Property	88	141	258	487	18.1	29.0	52.9
Other	517	95	399	1,011	51.1	9.4	39.5
Total Net Expenditure	6,454	3,037	2,271	11,762	54.9	25.8	19.3

SOURCE: Dominion Bureau of Statistics, A Consolidation of Public Finance Statistics, Municipalities, Provinces and The Government of Canada, 1961.

APPENDIX C

FEDERAL GOVERNMENT EXPENDITURES: NATIONAL ACCOUNTS
BASIS, BUDGETARY, NON-BUDGETARY, GRANTS TO PROVINCES,
LOANS AND GUARANTEES, AND EXPENDITURES OF FEDERAL GOVERNMENT
ENTERPRISES

TABLE C - I

FEDERAL EXPENDITURE BY MAJOR ECONOMIC CATEGORY

AS PERCENTAGE OF TOTAL AND AS PERCENTAGE OF

GROSS NATIONAL PRODUCT

(National Accounts basis)

Economic Category	1956			1963		
	\$ Million	% of Total	% of G.N.P.	\$ Million	% of Total	% of G.N.P.
Goods and Services	2,683	53.3	8.8	2,927	39.4	6.8
Defence	1,802	35.8	5.9	1,576	21.2	3.7
Other	881	17.5	2.9	1,351	18.2	3.1
Transfer Payments and Subsidies	1,866	37.1	6.1	3,340	44.9	7.8
Transfers to other levels of government	485	9.6	1.6	1,165	15.7	2.7
Total Expenditure	5,034	100.0	16.5	7,432	100.0	17.3
Gross National Product	30,585			43,007		

SOURCE: Dominion Bureau of Statistics, National Accounts, Income and Expenditure, 1961 and 1963.

TABLE C - II

FEDERAL EXPENDITURE BY FUNCTION AND
ECONOMIC CATEGORY 1961 - 62
(NATIONAL ACCOUNTS BASIS IN \$ MILLION)

Function	Total		Economic Category				
			Goods and Services		Transfer	Subsidies	Transfers Non-
			Salaries and Wages	Other	Payments	to Business ^a	to other levels of gov't
							Relevant items ^b
Defence Services and Mutual Aid	1,648.6	743.1	902.0	.1	-	1.6	1.8
Veterans Pensions and other benefits	337.9	50.3	28.6	251.5	-	-	7.4
General Government	287.1	139.1	145.6	-	-	-	2.3
Protection of Persons and Property	88.9	58.3	30.5	-	-	-	.1
Transportation and Communications	430.3	64.3	197.5	.4	97.0	55.7	15.4
Health and Welfare	1,790.4	62.8	42.2	1,189.0	-	476.7	55.6
Recreation and Culture	32.0	16.3	13.0	.4	-	1.7	.6
Education	93.6	8.2	14.9	32.3	-	38.2	-
Natural Resources and Primary Industry	404.8	81.1	78.3	97.2	130.5	12.9	4.9

TABLE C - II -- Concluded

Function	Total		Economic Category				
	Goods and Services Salaries and Wages	Other	Transfer Payments	Subsidies to Business ^a	Transfers to other levels of gov't	Non- Relevant items ^b	
Trade and Industrial Development	13.6	5.9	7.7	-	-	-	-
Debt Charges	839.0	2.4	802.9	-	-	-	13.7
Payments to Government Enterprises	170.9	-	-	-	-	-	170.9
Payments to Provincial and Municipal Governments ^c	567.3	-	-	-	-	567.3	-
Other	473.1	88.9	114.5	12.1	-	32.0	225.7
Total	7,177.5	1,318.3	1,577.3	2,350.9	227.5	1,186.1	518.3
Percentage of Total	100.0	18.4	21.9	32.8	3.2	16.5	7.2

^aThese consist mainly of production and consumption subsidies made with a view to price stabilization.

^bThese are expenditures which do not enter into the National Accounts. Included herein are purchase of land and used fixed assets. Capital assistance to industry is also shown here, since in the National Accounts framework, the gross capital expenditures made by industry are already included in the category of business gross fixed capital formation.

^cDoes not include grants for specific purposes.

SOURCE: Dominion Bureau of Statistics, Financial Statistics of the Government of Canada, 1961.

TABLE C - III

BUDGETARY EXPENDITURE CLASSIFIED BY FUNCTION

(\$ Million)

Function	Fiscal Year Ending March 31					
	1956		1960		1964	
	Amount	Per Cent	Amount	Per Cent	Amount	Per Cent
Defence	1,769	39.9	1,537	26.9	1,723	25.1
Health, Welfare and Social Security	618	13.9	947	16.6	1,417	20.6
Public debt charges	514	11.6	784	13.7	994	14.5
Payments to provincial and municipal govts.	359	8.1	543	9.5	290	4.2
Veterans Affairs	249	5.6	288	5.1	334	4.9
Transportation and Communication	341	7.7	633	11.1	786	11.4
Resources and Industrial Development	245	5.5	478	8.4	596	8.7
Education	10	.2	36	.6	182	2.6
International Co-operation	33	.8	83	1.5	72	1.0
General government	291	6.6	368	6.5	466	6.8
Unclassified	5	.1	7	.1	13	.2
Total Budgetary Expenditure	4,434	100.0	5,704	100.0	6,873	100.0
Old Age Security Fund Expenditure	353		575		808	
TOTAL	4,787		6,279		7,681	

SOURCE: Public Accounts of Canada, 1960, 1964.

TABLE C - IV

BUDGETARY AND NON-BUDGETARY TRANSACTIONS

	Fiscal Year Ended March 31	
	1964	1965 (Estimated)
<u>Budgetary Transactions</u>		
Revenue	6,253.2	7,136.0
Expenditure	-6,872.4	-7,219.0
Deficit	-619.2	-83.0
<u>Non-Budgetary Receipts and Credits (Net)</u>		
Repayments of loans, investments and advances		
Agricultural commodities stabilization account	75.0	38.0
Northern Ontario Pipe Line Crown Corporation	110.6	—
St. Lawrence Seaway Authority	-24.9	6.4
Old Age Security fund	-58.3	64.0
Other	<u>10.1</u>	<u>6.2</u>
	112.5	114.6
Annuities, insurance, and pension accounts	132.3	304.3
Public service super- annuation account	215.7	218.0
Canadian forces super- annuation account	<u>36.0</u>	<u>30.7</u>
Other	384.0	553.0
Other receipts and credits		
Outstanding treasury cheques	53.3	20.2
Accounts payable	75.3	72.5
Provincial tax collection agreements account	-2.7	52.4

TABLE C - IV -- Continued

	<u>1964</u>	<u>1965</u>
Unarmortized loan flotation costs	7.9	11.6
Interest due and outstanding	12.4	12.1
Interest accrued	<u>19.0</u>	<u>19.0</u>
	165.2	187.8
Total Receipts and Credits	661.7	855.4

Non-Budgetary Disbursements and Charges (Net)

Loans, investments, and advances

Atomic Energy of Canada Ltd.	0.4	13.0
Canadian Broadcasting Corporation	—	14.2
Canadian National Railways (including Air Canada)	-28.4	23.3
Canadian Overseas Telecommunication Corporation	6.2	0.8
Central Mortgage and Housing Corporation	113.3	221.0
Export Credits Insurance Corporation	23.4	33.8
Farm Credit Corporation	69.9	102.4
National Capital Commission	12.1	11.6
National Harbours Board	5.5	2.6
Northern Canada Power Commission	3.4	6.4
Columbia River Development	—	219.4
Exchange fund	-135.0	20.0
National governments	-15.1	11.3
Stockpiling of uranium concentrates	13.5	10.8
Subscription to international development association	—	7.9

TABLE C - IV -- Concluded

	<u>1964</u>	<u>1965</u>
Loans to provinces	-0.5	5.8
Veterans land act advances	21.0	14.2
Municipal Development and Loan Board	<u>-</u>	<u>7.5</u>
	89.7	726.0

Other disbursements and charges

Non-interest bearing notes payable on demand	170.3	219.1
Cash in hands of collectors	21.5	13.4
Unamortized portions of actuarial deficiencies		
Public service super- annuation account	-	159.3
Canadian forces super- annuation account	-	60.0
R.C.M.P. superannuation account	-	2.9
Other	<u>43.5</u>	<u>19.3</u>
	235.3	474.0
Total disbursements and charges	325.0	1,200.0
Overall cash requirement (-) to be financed by increase in unmatured debt or decrease in cash balances	-282.5	-427.6

SOURCE: House of Commons, Budget Papers, 1965 - 66.

TABLE C - V

FEDERAL CONTRIBUTIONS TO PROVINCES,
MUNICIPALITIES AND TERRITORIES
(\$ Million)

	Fiscal Year		
	1955	1962	1965
A. Payments To Provinces			
<u>Unconditional Grants</u>			
Tax rentals	372.4	312.6	-
Equalization	-	162.6	215.1
Stabilization	-	3.1	-
Share of federal estate tax	-	-	40.1
Atlantic Provinces adjustment grant	-	25.0	35.0
Newfoundland additional grant	-	8.0	8.0
50% share of income tax on power utilities	7.3	6.4	10.6
Statutory subsidies	20.3	23.5	23.6
Other	4.0	-	6.0
Total Unconditional Grants	359.0	541.1	338.4
<u>Conditional Grants</u>			
Recreation and Culture	.2	1.7	1.7
Hospital insurance	.	283.2	419.0
Other health	31.8	49.0	50.7

TABLE C - V- Concluded

Fiscal Year

	1955	1962	1965
Welfare	24.2	143.6	189.4
Education	4.4	35.9	100.3
Transportation	18.5	52.6	72.2
Agriculture	.9	5.4	12.8
Other natural resources	2.2	7.4	18.2
Civil defence	.5	3.1	5.6
Municipal winter works	—	24.2	30.0
National centennial	—	—	2.2
Other	<u>.4</u>	<u>.4</u>	<u>.2</u>
Total Conditional Grants	83.1	606.5	902.3
Total Payments to Provinces	442.1	1,147.6	1,240.7
B. Payments to Municipalities			
Grants in lieu of property taxes	3.4	25.1	30.3
Conditional grants	<u>1.4</u>	<u>11.0</u>	<u>30.3</u>
Total	4.8	36.1	53.3
C. Payments to Territories			
Statutory subsidies and tax rental	.6	1.1	5.0
Conditional grants	<u>.3</u>	<u>1.3</u>	<u>2.7</u>
Total	<u>.9</u>	<u>2.4</u>	<u>7.7</u>
Total Federal Payments	<u>447.8</u>	<u>1,186.1</u>	<u>1,301.7</u>

SOURCE: Canadian Tax Foundation, The National Finances, 1964 - 65, p. 124, Dominion Bureau of Statistics, Financial Statistics of the Government of Canada, 1961.

TABLE C - VI

FEDERAL NON-BUDGETARY LOAN AND CREDIT TRANSACTIONS

FOR FISCAL YEAR ENDING NEAREST DECEMBER 31

Transaction	\$ Million	
	1961	1963
A. Direct Loans by		
Farm Credit Corporation	68.6	108.0
Industrial Development Bank	71.2	80.0
Central Mortgage and Housing Corporation		
Mortgage loans under the National Housing Act	263.4	302.0
University housing projects	24.0	27.6
Municipal sewage treatment projects	39.9	36.0
Urban redevelopment	5.0	3.2
Municipal Development and Loan Fund	a	2.0
	332.3	370.8
Export Credits Insurance Corporation	42.1	—
B. Guarantees and Insurance		
Farm Improvement Loans Act	108.1	118.1
Small Business Loans Act	23.6	25.7
Fisheries Improvement Loans Act	.3	—

TABLE C - VI -- Concluded

Transaction	\$ Million	
	1961	1963
Central Mortgage and Housing Corporation		
Mortgage loans through approved lenders	306.4	385.0
Guarantee bank loans for home improvements	<u>42.6</u>	<u>36.7</u>
	349.0	421.7
Export Credits Insurance Corporation	174.9 ^b	287.9 ^b

^aLoans from the Municipal Development and Loan Fund began in November 1963.

^bLiabilities of the government under the policies in effect at the end of the fiscal year.

SOURCE: Central Mortgage and Housing Corporation, Annual Report, 1963; Department of Finance, Farm Improvements Loan Act, Annual Report, 1963; Department of Finance, Small Business Loans Act, Annual Report, 1963; Industrial Development Bank, Report of the President and Statement of Accounts, 1964; Canadian Tax Foundation, National Finances, 1961 - 62, 1963 - 64; House of Commons, Budget Papers, 1965 - 66.

Table C - VI sets out some of the major loan and credit operations of the federal government and its agencies. The four agencies mentioned, namely, the Farm Credit Corporation, the Industrial Development Bank, the Central Mortgage and Housing Corporation, and the Export Credits Insurance Corporation are federal crown corporations established for the purpose of making credit available to private interests. The Farm Credit Corporation is authorized to make long-term loans to farmers for purposes of acquiring land and equipment, and for farm improvements. The Industrial Development Bank was created for the purpose of providing capital assistance to small and medium industrial enterprises when other means of finance were not available. The Central Mortgage and Housing Corporation makes direct loans to home owners, under the provisions of the National Housing Act, to municipalities for sewage treatment projects and urban redevelopment, and is responsible for administering the Municipal Development and Loan Fund. The Central Mortgage and Housing Corporation is also authorized to insure mortgage loans and finances made by approved lenders for home ownership and rental housing, and to guarantee bank loans for home improvements. The Export Credits Insurance Corporation is responsible for insuring Canadian exporters against loss resulting from credit and political risks in foreign trade. The Corporation may also, with the authority of the Governor in Council, provide long-term financing for export sales of capital goods.

The government also conducts guarantee and insurance programs directly under established legislation. This includes operations under the Farm Improvements Loans Act, the Small Business Improvements Loans Act, and the Fisheries Improvement Loans Act. The purpose of the Farm Improvement Loans Act is to make available to farmers short and intermediate-term credit for the improvement and development of farms. The Act authorizes the Minister of Finance to guarantee each chartered bank against loss up to 10 percent of all Farm Improvement Loans during any lending period. The current lending period extends from June 1, 1962 to June 30, 1965, and the maximum that may be guaranteed in this period is set at \$400 million.

The Small Business Improvement Loans Act makes short-term credit available to proprietors of small business to assist them in financing capital improvements by authorizing the government to guarantee chartered banks against loss up to 10 percent of loans made by them. Assistance for capital improvements in the fishing industry is provided on similar terms by the Fisheries Improvement Loans Act.

TABLE C - VII

FEDERAL GOVERNMENT ENTERPRISES^a CURRENT

EXPENDITURE BY INDUSTRY FOR FISCAL YEAR

ENDED NEAREST TO DECEMBER 31, 1961

(\$ Million)

Expenditure	Manufacturing	Transportation, Communication and Other Utilities	Wholesale Trade	Finance, Insurance, Real Estate	Total ^b
Cost of goods and services sold from current operations					
Wages and salaries	33	554	3	13	602
Net drawings on (-) or additions to (+) inventories	12	2	-11	-	3
Other purchases of goods and services	244	371	699	10	1,324
Sub-total	289	927	691	23	1,929
Provision for depreciation	9	127	-	2	138
Interest on debt to					
(i) Federal govt.	-	30	-	72	102
(ii) Federal govt. enterprises	-	11	-	3	13
(iii) Other	-	69	13	-	82
Sub-total		110	13	75	197
Other current expenditure	1	4		1	5
Total Current Expenditure	299	1,168	704	101	2,269

^a Excludes Bank of Canada

TABLE C - VII Concluded

^b May not necessarily balance due to rounding.

SOURCE: Dominion Bureau of Statistics, Financial Statistics of Federal Government Enterprises, 1961.

APPENDIX D

THE CANADIAN BUDGETARY SYSTEM

This appendix consists of a description of the present budgetary system of the Government of Canada. It is concerned primarily with the expenditure side of the budget, and emphasis is placed on the expenditure classification scheme, the preparation of expenditure estimates within departments and their review by the Treasury Board and Parliament. Attention is focussed on some of the more recent developments that have taken place in financial organization and administrative procedure in the budgetary system.¹

A. Financial Structure And

General Budgetary Procedure

The financial structure of the Canadian government rests on a constitutional and statutory framework dating back to the British North America Act of 1867. This Act gave constitutional foundation to the principles of financing government basic to responsible government, while other necessary financial machinery and procedures were provided for by subsequent parliamentary legislation. Many of these financial practices had been developed earlier in the former Provinces of Canada and were simply carried forward.

Following Confederation revisions were required to keep pace with changing conditions and the increasing scale of government operations. By the end of the 1940's government organization and financial operations had expanded to the extent that it became necessary to review federal legislation and to consolidate in one statute, in simplified form, the provisions relating to financial organization and administration included in various earlier statutes. It was also considered desirable to put into statutory form certain practices which had developed and had been found to be convenient. The result was the passing of the Financial Administration Act by Parliament in 1951. This comprehensive piece of legislation covers procedures regarding the collection and disbursement of public funds and the organization and functions of the major financial agencies in the federal government.

Expenditure Control

The British North America Act

Section 53 of the British North America Act of 1867 provided that all financial bills, revenue and appropriation, must originate in the

¹The Royal Commission on Government Organization made various recommendations regarding financial organization and procedure in the federal government, and some of the changes that have been made have been in accordance with these recommendations.

House of Commons. But while the legislature was made responsible for authorizing financial measures, the executive was made responsible for the direction and execution of government finances. The Act carried a provision to this effect in Section 54:

It shall not be lawful for the House of Commons to adopt or pass any vote, Resolution, Address, or Bill for the appropriation of any part of the Public Revenue, or of any Tax or Impost, to any Purpose that has not been first recommended to that House by Message of the Governor General in the Session in which such Vote, Resolution, Address, or Bill is proposed.²

The British North America Act also provided for the earlier practice, which had been established for the Provinces of Canada by the Act of Union in 1840, that all public revenues collected were to form one Consolidated Revenue Fund from which appropriations were to be made by Parliament.

The British North America Act makes no mention of the Cabinet, but this body and its powers have developed following British parliamentary tradition. The Act vests executive power in the Queen represented by a Governor-General. The Governor-General is advised by a Council chosen by him and known as the Queen's Privy Council for Canada. The Privy Council consists of all cabinet ministers, past and present, as well as other persons who may be appointed as members. The active part of the Council is formed by current Cabinet Ministers who exercise the real executive power and whose formal collective decisions are presented in the form of Orders-in-Council. The formal Privy Council has virtually never met.

The Role of the Treasury Board

The Treasury Board, a committee of the Privy Council, was originally created by Order-in-Council in 1867 and placed on a statutory basis with the enactment of the Department of Finance Act in 1869. It was established as an executive arm of government to assist the Cabinet in its financial responsibilities. Charged with the supervision of "all matters relating to Finance, Revenue, and Expenditure, or Public Accounts which may be referred to it by the Council"³ it was to prove a major institution in the budgetary process of Canada.

Until recently the Treasury Board consisted of the Minister of Finance, as chairman, and "any five members of the Queen's Privy Council for Canada, who may be nominated from time to time by the Governor in Council"⁴ As a result of a recent change in the organization of

²Statutes, 30-31 Vict. c.3, s.54.

³Statutes of Canada, 32-33 Vict. c.4, s.4.

⁴Ibid., 15-16 Geo. VI, c.12, s.3.

the Treasury Board, the Board is now presided over by the President of the Privy Council. He is named to be President of the Treasury Board. The Board still consists of five other nominated members and these members are, and always have been, Cabinet Ministers. The Board is served by a staff directed by an officer designated to be secretary of the Treasury Board.

The Financial Administration Act clarified and broadened the functions of the Treasury Board as stipulated in the Department of Finance Act. Its general function is given as follows:

The Treasury Board shall act as a committee of the Queen's Privy Council for Canada on all matters relating to finance, revenues, estimates, expenditures and financial commitments, accounts, establishments, the terms and conditions of employment of persons in public service, and general administrative policy in the public service referred to the Board by the Governor in Council or on which the Board considers it desirable to report to the Governor in Council, or on which the Board considers it necessary to act under powers conferred by this or any other Act.⁵

The Treasury Board was also given powers for prescribing the manner and form in which government accounts were to be kept and for making regulations regarding "the collection, management and administration of, and the accounting for public money".⁶

The Cabinet and the Treasury Board are the policy making and budget control bodies of the government respectively. The general magnitude of the budget is decided by the Cabinet when it determines general policy in the various fields of government activity. The Treasury Board exercises the detailed central control over the expenditures of the various departments, which includes establishing priorities and coordinating the expenditure programs and activities of the departments.

As a first step in the preparation of the budget each government department or agency is required to submit to the Treasury Board estimates of the cost of each activity or service that it is planning or anticipating for the coming fiscal year. Prior to the submission of the expenditure estimates by the departments, however, a review of each department is conducted by what is known as an Establishment Review Committee composed of a representative from the Civil Service Commission, a representative from the Treasury Board staff, and a representative from the department concerned. This committee examines the establishment of each department to determine if all existing staff is fully utilized and necessary, and to review the new proposals of the departments for additional staff as a result of extended or new programs. The Treasury Board representative

⁵ Ibid s.5.

⁶ Ibid s.7.

indicates government policy for the coming year, and with this in consideration the committee reviews the various proposals of a department and decides on the number of new positions that will be recommended to the Treasury Board for approval.

The Treasury Board indicates the commencement of the estimates process by means of a formal letter of instruction to all deputy heads of the various departments. This letter is generally issued in the beginning of July and departments are required to submit their expenditure plans by November. The call for estimates is accompanied by an outline of government financial policy for the coming year and requests that departments take this policy into consideration when determining their expenditure plans. At one time the letter of instruction was also accompanied by a description of the desired form in which the estimates were to be submitted. In 1956 this procedure was abandoned however when the Treasury Board staff prepared a "Manual of Estimates"⁷ which was distributed to the departments in an attempt to facilitate clearer understanding of the procedures to be followed in the preparation of departmental estimates.

The departmental expenditure estimates are prepared under the direction of the deputy minister, and after being reviewed and approved by the Minister of the department concerned they are forwarded to the Treasury Board. The Treasury Board staff generally conducts a review of the estimates from two points of view: cost and policy. With regard to cost the staff must be satisfied that all expenditure items are reasonable for the proposed program. The policy review is conducted to ensure that all new programs have been approved in principle by Cabinet or Treasury Board prior to their inclusion in the estimates.

After tabulating the estimates in the prescribed form and assembling supporting data, the secretariat transmits them to the President of the Treasury Board. The Board meets daily for approximately three weeks in late November and early December to examine and discuss the estimates. The Board may reject any expenditure proposal it considers not in line with the broadly stated budget objective and may postpone or cancel proposals of lesser priority. During the course of its review the Board may call on the ministers of the various departments to explain and justify their requests. This type of review endeavours to establish priorities among proposed expenditures, to ensure that departmental expenditure proposals are held within approved government policies, and to ensure that departments follow economical practices.

Finally the estimates as a whole are submitted to the Cabinet for

⁷ See Department of Finance, Estimates Manual (Ottawa; Queen's Printer, 1956).

a final general review,⁸ which includes their comparison with anticipated revenues. The traditional approval by the Governor-General is also required before the estimates are tabled in the House of Commons.

The total expenditure estimates of all departments are tabled in one document called Estimates, or what is often referred to as the Estimates Blue Book. The estimates appearing in this document are referred to as the main estimates for the approaching fiscal year, but they are by no means the only expenditure estimates to be submitted to Parliament. During the course of the fiscal year several sets of additional so-called supplementary estimates are usually presented. As each department must prepare at the beginning of the current fiscal year its estimates of expenditures for the following fiscal year, the main estimates so prepared are frequently incomplete. A department may discover that its estimates did not provide for items or projects not previously anticipated or that some of the estimates submitted for other items were insufficient. This is certain to be the case if there is a change in government policy calling for increased government activity or services and consequently increased expenditure. The department concerned must then estimate these expenditures and submit the estimates to Parliament. Following the first set of supplementary estimates the department may still find that the funds appropriated to it are insufficient for the fiscal year and may submit still further requests. These supplementary estimates provide for a certain degree of flexibility in the expenditure side of the budget.

Parliamentary Appropriation

The main expenditure estimates are usually tabled in the House of Commons in the beginning of February. The estimates are examined by the Committee of Supply, which is the House of Commons sitting as a committee of the whole. In the process of considering departmental estimates, the House of Commons makes available to each of the members of the House a copy of the Estimates Blue Book together with tabulations of supplementary estimates. In the Blue Book the various government departments and agencies appear in alphabetical order. Expenditures in a department are grouped into items and each such item is designated by an appropriation or vote number. The estimates are considered item by item and each item requires a resolution and a vote. The Minister of each department is responsible for steering his department's estimates through the House and is expected to be present to

⁸In practice the Treasury Board is under the control of the Cabinet which may amend or revoke any action of the Board. The President of the Treasury Board must present the financial plans (expenditure estimates) before the Cabinet as a whole, but if he has the other five members of the Board sharing his views then he is usually in a strong position with respect to convincing the remaining members of the Cabinet. Consequently the decisions of the Treasury Board concerning expenditures will usually be accepted by the Cabinet.

answer any questions put forth by the opposition or by the members of his own party regarding departmental policy or any of the individual items. Collectively the cabinet ministers are responsible for the general budget of expenditures, but individually they are responsible for the management of their departments and the administration of the expenditures proposed. The Minister, in explaining and defending the estimates of his department, usually has the deputy minister and one or two prominent officials from his department appear in the House in an advisory capacity to assist him. The Deputy Speaker of the House, acting as chairman of the Committee of Supply, asks whether item "X" shall "carry", and if no member has any opposition or comment to voice regarding the item it is "carried" and the chairman proceeds to the next item.

Consideration of the estimates presents an opportunity for Parliament to review government policy and programs for which the expenditures are required. The debates are generally detailed and time consuming, and in the past have occupied a fairly large proportion of the Parliamentary time-table.

The Committee of Supply passes resolutions covering expenditure items and reports to the House. These resolutions are then referred to the Committee of Ways and Means which is also a committee of the whole. The Committee of Ways and Means considers the resolutions regarding expenditure estimates for the purpose of appropriating these amounts out of the Consolidated Revenue Fund. This is a formal matter and does not occupy very much time, for the Committee cannot debate what has been decided in Supply or amend the resolutions in any way. The Committee of Ways and Means then reports back to the House and the supply or appropriation bill is introduced. The bill goes through the three readings of the House and after being considered by the Senate⁹ is signed by the Governor-General and becomes an Act of Parliament. The supply items in the bill become grants. These grants, however, are not mandatory. They are released by Order-in-Council and the Cabinet has the authority to withhold any grant from a department even though the funds have been appropriated. Thus no payment is made for an appropriation out of the Consolidated Revenue Fund unless a warrant prepared by the Cabinet has been signed by the Governor-General authorizing expenditures to be charged against the appropriation. This process, known as the release of supply, is provided for under Section 26 of the Financial Administration Act:

Where an appropriation is made for any purpose in any Act of Parliament for granting to His Majesty any sum of money to defray expenses of the

⁹The role of the Senate is a minor one in regard to the budgetary procedure. Money bills are considered and passed by the Senate but the British North America Act provides that money measures must originate in the House of Commons and the House has held that this is its sole right and is not to be encroached upon by the Senate. The Senate may discuss money matters and the policies involved and it may reject or amend money bills although it very seldom does so.

public service for a fiscal year, no payment shall be made pursuant to that appropriation out of the Consolidated Revenue Fund unless a warrant, prepared on the order of the Governor-in-Council has been signed by the Governor-General authorizing expenditures to be charged against the appropriation, but no payments in excess of the amount of expenditures so authorized shall be made.¹⁰

Since the main estimates are not appropriated by Parliament until some time after the beginning of the fiscal year on April 1st, and since appropriations for the preceding fiscal year lapse on March 31st, provision must be made to carry on the functions of government until such time as the main supply bill is enacted. This is provided for by Interim Supply bills which grant a fraction of each of the tabled estimates, usually one twelfth or one sixth, to meet expenses in the new fiscal year until the main supply bill is passed. An Interim Supply act is complete in itself and remains operative even though Parliament may refuse to appropriate the main estimates of any one or more of the departments concerned.

Besides those expenditures for which Parliament makes direct annual appropriations there are also other expenditures which appear in the budgetary estimates which are not annually appropriated by Parliament. These are expenditures authorized by statute or what are known as statutory appropriations, which Parliament has agreed should not be subject to annual review and debate. Examples of these statutory appropriations are the subsidies to provinces as provided for by the British North America Act and its amendments and the interest on the public debt. Changes in these expenditures require a statutory amendment.

With one exception, the federal government adheres to the provision of the British North America Act that any appropriation of public money out of the Consolidated Revenue Fund may be made only on the authority of Parliament. This exception relates to the use of Governor-General's warrants for meeting unforeseen and emergency expenditures. The Consolidated Revenue and Audit Act of 1878 authorized the use of Governor-General's warrants and this provision was re-enacted in Section 28 of the Financial Administration Act. The Governor-General has this authority only when Parliament is not in session or is adjourned "sine die." The Minister of Finance reports to the Governor-in-Council that there is no appropriation for an expenditure which is urgently needed. The Governor-in-Council may then order the preparation of a special warrant for the Governor-General's signature authorizing the payment of the estimated amount required. Such warrants, however, must be presented before the House of Commons by the Minister of Finance within fifteen days after the commencement of the next session of Parliament.¹¹ An amendment to the Financial Administration Act in 1958 stipulated that amounts granted by warrants were to be "included in and

¹⁰ Statutes, 15-16 Geo. VI, c.12.

¹¹ Ibid.

not to be in addition to" the next appropriation act.¹² Expenditures covered by warrants therefore must be subsequently approved by Parliament.

The Role of The Comptroller of The Treasury

The issue and control of disbursements of public funds in accordance with authorized appropriations is the responsibility of the Comptroller of the Treasury. The office of the Comptroller, which is within the Department of Finance, was first created in 1931 with the revision of the Consolidated Revenue and Audit Act of 1878 which governed the management of revenue and the auditing of public accounts.¹³

The Comptroller, appointed by the Governor-in-Council, has a two fold function. First, he is responsible for maintaining the accounts of the government. In this capacity he has free access to all material relating to the accounts of every department and may furthermore examine their accounting practices. From the records maintained of the financial transactions the annual Public Accounts of Canada are compiled, their tabulation following closely the form in which the expenditure estimates are presented.¹⁴ Secondly, the Comptroller is the expenditure control officer for the government. The Financial Administration Act, which repealed the Act of 1931 and brought the functions of the Comptroller up to date, stipulates that no money appropriated by Parliament can be released from the Consolidated Revenue Fund to a department except on requisition from the Minister of the Department concerned. It is the responsibility of the Comptroller to ensure that a requisition is in accordance with an appropriation before he releases the requested funds. He has the statutory right to reject the requisition if he is of the opinion that the payment would not be a lawful charge against the appropriation or would result in an expenditure in excess of the appropriation.¹⁵ This pre-audit practice by the Comptroller ensures that no expenditure can be made which was not authorized by parliament and which would therefore not be in accordance with pre-determined policy.

Revenue Determination and The Budget Speech

Government expenditures are based on planned activities and

¹²Statutes, 7 Elizabeth II, c.31.

For some background on the development and use of Governor-General's warrants, see Norman Ward, The Public Purse (Toronto: University of Toronto Press, 1964).

¹³Statutes, 21-22 Geo. V, c.27.

¹⁴See Canada, Department of Finance, Public Accounts of Canada for the Fiscal Year ended March 31, 1963, Vol. I, II, III.

¹⁵Statutes, 15-16 Geo. VI, c.12.

services for which fairly accurate estimates of the expenditures to be incurred can be made. Attempts at estimating government revenues, however, and the subsequent planning of taxation policies prove to be much more difficult due to fluctuations in the level of economic activity. As former Finance Minister D.M. Fleming stated in his Budget Speech of March 31, 1960, "Revenue forecasting, as I have observed on previous occasions, always presents formidable difficulties."¹⁶ In his budget speech of 1952 the then Minister of Finance, D.C. Abbott had similarly commented that "the problems of forecasting are closely tied to general economic trends which are not easy to predict."¹⁷

The determination of government revenues and taxation policy is thus closely related to forecasts of economic trends and developments. These forecasts are conducted by various government departments and agencies working in close liaison with the Department of Finance and include the Dominion Bureau of Statistics, the Bank of Canada, and the departments of Trade and Commerce, Labour, and Agriculture.¹⁸ From the

¹⁶Canada, House of Commons Debates, March 31, 1960, p. 2680.

¹⁷Ibid., April 8, 1952, p. 1247.

¹⁸Although forecasting of economic activity is a rather complex process some generalities regarding government forecasting can be observed. Within the Department of Finance are two main departmental divisions responsible for the preparation of forecast material: the Taxation Division and the Financial Affairs and Economic Analysis Division. The Taxation Division forecasts revenues, advises the Minister of Finance on taxation policy, and studies the possible effects of changes in existing tax rates. The Economic Analysis Division concerns itself with forecasting and reviewing the economic situation and preparing material on which fiscal decisions are made.

The Dominion Bureau of Statistics is continually conducting sample surveys and gathering statistical data regarding economic activity in Canada for national accounting purposes. The main sources of these data fall into two general classes. The first and more important is based on questionnaires mailed from the Bureau to the business community, and the second is based on the administrative records of various government departments and agencies. These surveys include annual and monthly surveys of manufacturing, mining, fishing, and agriculture, surveys of retail and wholesale establishments, of inventories and shipments, of realized and intended capital investment, and surveys of the labor force and unemployment. From these surveys estimates can be made of wages and salaries, farm income, personal expenditures on consumer goods and services, investment in housing and construction, machinery, equipment and inventories, and trends can be ascertained.

The Economics Branch of the Department of Trade and Commerce also carries on a continuous review of the economic situation in the country by making appraisals of current and prospective developments and conducting studies on specific economic matters.

information thus obtained, the Taxation Division of the Department of Finance forms conclusions as to the yield of various revenue sources in the coming fiscal year and estimates the effects upon revenues of any tax changes that are proposed. Such proposals are presented annually before the House of Commons by the Minister of Finance in his budget speech and appear as resolutions to amend existing tax statutes.

The budget speech of the Minister of Finance brings together expenditures and revenues and introduces proposals of changes in the tax structure and tax rates. There is no set date for the presentation of the budget speech, although it is normally delivered shortly following the commencement of the fiscal year. Most budget speeches follow a standard pattern with regard to form and presentation. They usually begin with a general review of the economic and financial conditions within the country during the previous year, with emphasis on the level of economic activity, its stability and growth, interest rates, capital requirements, the balance of payments and Canada's position in international trade. The second phase of the budget speech consists of a brief review of the government accounts and the financial operations of the government in the past fiscal year. The third section outlines the general level of expected expenditures and revenues. Estimates of revenues are compared with the expenditure estimates and the size of the expected surplus or deficit is predicted. The fourth and final section of the budget consists of an outline of the government's proposals regarding tax and tariff changes and the effect these changes are expected to have on the budget and on the economy.

Following the presentation of the budget speech in the House, a debate is held on the budget which continues for approximately six days. This provides an excellent opportunity for parliamentary members to discuss government policy in financial and economic matters such as unemployment, the price level, taxation policy, the national debt and bond issues, economic growth, etc.

The budget speech is accompanied and supplemented by the Budget White Papers. Their significance can be observed from the following comment made by former Finance Minister Fleming in his budget speech of June 20, 1961:

The white paper also contains a full account of the economic events of 1960. It includes an analysis of the more significant longer term developments in Canada and in the world as a whole related to the Canadian situation. I commend this analysis to the careful study of the honourable members.¹⁹

The budget papers are composed chiefly of elaborate and up-to-date tables of economic data. The first part consists of a review of national product and income, personal income, savings, investment, revenue and expenditure of all governments, and financial developments in the country. The second section presents the highlights of government financial operations for the previous fiscal year including a review of budgetary expenditures and

¹⁹Debates, June 20, 1961, p. 6640.

revenues, a summary of assets and liabilities, and an analysis of the government's cash position and the public debt.

Proposals for tax changes are usually made only during the annual presentation of the budget.²⁰ The resolutions providing for changes in tax legislation are considered by the Committee of Ways and Means following the budget debate, and when all resolutions have been considered and carried by the Committee they are reported to the House of Commons.²¹ These resolutions are incorporated into tax amendment bills and are dealt with in the same manner as all government legislation. The tax changes, however, become effective immediately on the introduction of the resolutions in Parliament during the budget speech.

The Department of National Revenue is responsible for the administration of tax legislation, that is, the control and management of the collection of customs duties and all internal taxes.²² The Department consists of three divisions; the Customs Division, responsible for the collection of import duties; the Excise Division, responsible for sales and excise taxation; and the Taxation Division, responsible for the collection of personal and corporation income taxes and succession duties.

The Post-Audit

Following the collection and disbursement of public funds, it is the duty of the Auditor General to conduct a post-audit of the financial transactions and to report his findings to the House of Commons.²³ The

²⁰There have been exceptions to this, such as Finance Minister Fleming's supplementary or "baby" budgets on December 6, 1957 and on December 20, 1960.

²¹For the technicalities of this procedure, see W.F. Dawson, Procedure In The Canadian House of Commons (Toronto: University of Toronto Press, 1962), p. 216-217.

²²The Department of National Revenue was established in 1927 by the Department of National Revenue Act. Previously the collection of public funds was the responsibility of the Department of Customs and Excise. The Act of 1927 reorganized the old department and changed its title to the Department of National Revenue.

²³The audit of government accounts was provided for immediately after Confederation with the enactment of the Consolidated Revenue and Audit Act in 1867. This Act established the position of Auditor, assisted by a Board of Audit of which he was chairman. The Board consisted of eight members, mostly deputy ministers of various departments, appointed by the Governor in Council and supervised by the Minister of Finance. In 1878 an amendment to the Act abolished the Board of Audit and created the office of Auditor General. Previously the office of Auditor was within the Department of Finance but the Act of 1878 made the Auditor General a parliamentary officer independent of the Department of Finance and the executive. The function of the Auditor-

Auditor General is an officer of Parliament and in this respect he has often been referred to as the "financial watch-dog of Parliament."²⁴ He is appointed by the Governor-in-Council and holds office during good behaviour. The Financial Administration Act requires that the Auditor

call attention to every case in which he has observed that

- (a) any officer or employee has wilfully or negligently omitted to collect or receive any money belonging to Canada,
- (b) any public money was not duly accounted for and paid into the Consolidated Revenue Fund,
- (c) any appropriation was exceeded or was applied to a purpose or in a manner not authorized by parliament,
- (d) an expenditure was not authorized or was not properly vouched or certified,
- (e) there has been a deficiency or loss through the fraud, default, or mistake or any person, or
- (f) a special warrant authorized the payment of any money, and to any other case that the Auditor General considers should be brought to the notice of the House of Commons.²⁵

It is through the post-audit process that the House of Commons receives a full accounting for the manner in which approved budgetary plans are administered. It is also the Auditor's duty to determine whether "the rules and procedures applied are sufficient to secure an effective check on the assessment, collection, and proper allocation of the revenue"²⁶ and to make any recommendations to Parliament of changes in rules and procedures that he feels are necessary.

The Auditor General's annual report is normally tabled in the House of Commons simultaneously with the Public Accounts to which it relates.²⁷ These two documents are then referred to the Public Accounts Committee for review. The Public Accounts Committee is a standing committee of the House of Commons and was created immediately following Confederation. The Committee consists of fifty members the majority of

General was to control the issue of public funds and examine the accounts after payment was made, his findings to be reported to the House of Commons. The Auditor General continued these two major roles of expenditure control until 1931 when an amendment to the Consolidated Revenue and Audit Act removed the function of pre-audit from the office of the Auditor General and placed it in the hands of the newly created Comptroller of the Treasury. For a detailed account of the early development of the office of the Auditor General, see Norman Ward, The Public Purse (Toronto: University of Toronto Press, 1964).

²⁴I. Stevenson, "Auditor General - Watchdog of Parliament," Canadian Chartered Accountant, (July - Dec. 1956) p. 399.

²⁵Statutes, 15-16 Geo. VI, c.12, s.70.

²⁶Ibid. s.67.

²⁷See Canada, Report of the Auditor General to the House of Commons, 1963.

which are members of the party in power. In connection with its function of examining and reporting on government financial transactions it may call before it not only the Auditor but other such officers as it believes necessary.²⁸

~~Non-Budgetary~~ Transactions

Government financing is not conducted entirely through the budget, for there are certain government transactions which do not appear in the budget but yet form an important element in the financial operations of the government and consequently affect the government's cash position. The Comptroller of the Treasury, H.R. Balls, has described the budgetary and non-budgetary accounts as follows:

The budgetary accounts are roughly analogous to the income accounts of business which record current income and current expense, and measure the magnitude of the consequential periodic profit and loss, while the non-budgetary accounts record those transactions which affect the government's asset and liability accounts.²⁹

Non-budgetary transactions arise from activities conducted through government agencies and trust funds, from loans to other governments, and from investments in international organizations. The former Minister of Finance, D.M. Fleming, had the following to say regarding the nature of such transactions in his budget speech of March 31, 1960:

In addition to the expenditures for administrative and other governmental services that are included in our budgetary accounts, we pay out each year substantial amounts of cash as loans to and investments in a wide variety of public undertakings. These outlays are not considered as budgetary expenditures as the principal is usually repaid, and in almost every case they earn interest or produce revenue for the government.

Against this we receive each year large amounts of cash that are not recorded as budgetary revenue. For the most part these consist of repayments of loans made in previous years and money received by the government as net premiums contributions and earnings in connection with annuities, insurance, or pension funds.³⁰

²⁸For a more detailed account of the organization and functioning of the Public Accounts Committee, see Supra, pp.230 - 232. Also, see Ward, op. cit.

²⁹H.R. Balls, "The Public Accounts, Their Purposes and Factors Affecting Their Form: An Administrative View," Canadian Public Administration, VII (December, 1964), p. 438.

³⁰Debates, March 31, 1960, p. 2681.

Government trust funds are special funds which are excluded from budgetary tabulations except to the extent that they involve government contributions. The most significant of these funds are the Old Age Security Fund³¹ and the Unemployment Insurance Fund. The Old Age Security Fund is financed by so-called Old Age Security taxes consisting of a three per cent sales tax, a four per cent tax on personal income,³² and a three per cent tax on corporation income. These revenues are considered non-budgetary. Deficits in the fund either appear as a budgetary charge or are financed by temporary loans. The Unemployment Insurance Fund is financed by equal contributions from employees and employers, by interest earned on investment, and by the government contribution of an amount equal to one-fifth of the combined employee-employer contributions. Contributions by employees and employers are treated as non-budgetary revenue while the government's contribution is granted under a statutory appropriation and is included in the budgetary estimates of expenditure. Loans to the fund are not usually charged to budgetary expenditures, as it is expected they will be repaid in periods when contributions exceed payments.

A second major category of non-budgetary transactions consists of loans and advances to, and repayments by national, provincial, and municipal governments and international organizations. These loans are provided for by Parliamentary statutes rather than by budgetary appropriations. However, direct contributions to international economic and special aid programs, such as contributions under the Colombo Plan, which are not subject to repayment are authorized by Parliamentary appropriations and are included among budgetary expenditures.

A considerable portion of non-budgetary transactions consist of loans and advances to, and investments in, crown corporations, and receipts from these corporations in the form of repayments of loans. The operations of some of these crown corporations are fairly extensive, and their financial transactions total a larger sum than that of some government departments.

Partly because of the nature of the functions performed by them, government corporations have acquired a considerable degree of diversity in form and procedure. The Financial Administration Act defined a crown corporation as "a corporation that is ultimately accountable, through a Minister to Parliament for the conduct of its affairs."³³ The Act established a uniform measure of financial control over these corporations and provided for their annual reporting to Parliament. The corporations were grouped into three classes, namely, departmental, agency, and proprietary corporations. This classification was based primarily on

³¹For the fiscal year 1964-65 it was expected that revenues for the fund would amount to \$900 million, while approximately \$885 million would be paid out in pensions.

³²Increased from three per cent to four per cent effective Jan. 1, 1964.

³³Statutes, 15-16 Geo. VI, c.12, s.76.

two factors; the extent of financial independence and the nature of the function performed.

Departmental corporations are those crown corporations which are responsible for administrative, supervisory, or regulatory services of a governmental nature. They are generally treated similarly to a government department, and their financial transactions are accounted for as budgetary revenues and expenditures.

Agency corporations are generally responsible for the management of trading and service operations or for the management of procurement and construction activities. They are not included in the general government budget but have separate budgets. The methods of financing include parliamentary appropriations, statutory grants, and corporate operational income.

Proprietary corporations manage financial, commercial, or industrial operations and are normally expected to finance themselves from the sale of goods and services. Should a deficit occur it is usually covered by a parliamentary appropriation. Proprietary corporations are the most autonomous of Canadian crown corporations. Agency corporations are required to submit an operating budget to Parliament, but proprietary corporations are not required to do so, although both types of corporations must submit their capital budgets. With regard to the submission of operating budgets, the government justified its position as follows:

An agency corporation is an agent of one of the departments. But these other corporations, which are set up independent of the operations of any department, may very often. . . have directors who are chosen from the business life of the country. Some of these businesses are very successful. These corporations should have a certain degree of independence such as they would have if they were private corporations.³⁴

Five crown corporations, namely, the Bank of Canada, The Canadian Wheat Board, the Industrial Development Bank, the Northern Ontario Pipe Line Corporation, and the Canadian World Exhibition Corporation, do not belong to the above three categories but operate under their own Acts. They have separate budgets like the proprietary corporations.

Loans and advances to crown corporations bear interest which appears as budgetary non-tax revenue, but the repayments of these loans are considered non-budgetary receipts. Section 82 of the Financial Administration Act outlines the regulations governing loans to crown corporations. These loans are made from the Consolidated Revenue Fund by the Minister of Finance at the request of the appropriate Minister, but are subject to the approval of the Governor-in-Council. The Act further stipulates that "a report of every loan to a corporation under this section shall be laid by the Minister of Finance before

³⁴Debates, December 15, 1951, p. 2007.

Parliament within fifteen days after it is made."³⁵

The audit of the accounts of departmental corporations is the responsibility of the Auditor General. With regard to the accounts of agency and proprietary corporations the Financial Administration Act provides that if,

. . . no provision is made in any Act for the appointment of an auditor to audit the accounts and financial transactions of the corporation. . . the Governor in Council shall designate a person to audit the accounts and financial transactions. . .³⁶

Furthermore, each corporation is required by the Act to prepare a financial report at the termination of each financial year which is to include a balance sheet and a statement of income and expenses. The annual reports of the corporations describing their operations are to be submitted to the appropriate Ministers who are required to present them before Parliament.

B. Expenditure Classification And Review In The Canadian System

Present Classification Scheme

Organizational Units and Objects of Expenditure

The services and operations undertaken by the federal government are administered through units organized for this purpose, such as departments, agencies, and boards and their component branches and divisions. The expenditure classification scheme is based on organizational units, with the expenditures of the various units divided into more detailed categories illustrating the items or objects to be purchased.³⁷ The present form in which the expenditures are thus broken down into objects is known as the standard-objects-of-expenditure classification.

The government departments and agencies are organized along lines of major purposes to be served, such as defense, trade and commerce, transport, health and welfare, etc. The subdivisions of the departments

³⁵ Statutes, 15-16 Geo. VI, c.12, s.82.

³⁶ Ibid s.77.

³⁷ For an account of some of the various forms in which expenditures may be classified, see Jesse Burkhead, Government Budgeting (New York: Wiley and Sons, 1956), pp. 110-132.

For a discussion concerning some of the factors affecting the Canadian expenditure accounts, see H.R. Balls, "The Public Accounts, Their Purposes And Factors Affecting Their Form: An Administrative View," Canadian Public Administration, VII (December, 1964), pp. 422-441.

are in turn organized along the lines of the service or operation for which they are responsible and which relate to the general purpose. This so-called classification by purpose, however, is not completely adhered to, for the departments as they presently exist cut across these broad purpose lines. For instance, expenditures for highway construction may be found in the Department of Public Works as well as the Department of Transport. Various services and activities have been shifted from one department to another in the past presumably in an attempt to make each department more representative of the function it was established to perform. Since 1960 there have been approximately twenty transfers of activities between departments. Examples of some of these transfers are the carrying costs of temporary wheat reserves transferred from Agriculture to Trade and Commerce, and External Aid office from Trade and Commerce to External Affairs.

The Estimates Blue Book

The classification of expenditures by objects has been in effect in the Canadian budget since Confederation although the actual form has been altered to a certain extent over the years. Since the major revision in the form of the expenditure estimates which took place in 1938, several other revisions have been made. Nevertheless, the basic idea of presenting the estimates in the form of objects or items has remained intact. At present the expenditures are grouped into what has been adopted as Standard Objects of Expenditure and Special Categories. This is a fairly broad classification which was developed by the Treasury Board and which first appeared in the Estimates in the fiscal year 1951-52. It is illustrated in the adjoining table. There are 22 objects listed under the Standard Objects Classification and 11 items termed Special Categories. The Special Categories are of the nature that they could be classified under the Standard Objects, but it was thought that they were significant enough to warrant special mention. Each major expenditure in the estimates is sub-divided into these objects. The Objects and Special Categories are identified by the permanent numbers which have been assigned to them.

Prior to the revision in 1938, the estimates, as presented in the Estimates Blue Book, did not reflect the costs of the various services of government nor did they clearly indicate departmental responsibility for government operations. Portions of the expenditures of departments were found under various captions or appropriations of a general nature while other expenditures were assembled under obsolete headings which had no relationship to departmental responsibility as it then existed. Expenditures were grouped under general services rather than under administrative units such as departments. The expenditure classification for appropriation purposes took the form of such broad categories as "civil government." Certain expenditures of a department, such as administrative expenses, would be appropriated under this category while the remaining expenditures would be found under other categories. The result was that it was difficult to determine the cost of any particular activity or to determine departmental responsibility. The revision was intended to remove such obsolete headings as "Mail Subsidies and Steamship Subventions", "Pensions", "Miscellaneous", etc.³⁸ and to

³⁸See Canada, Estimates for the Fiscal Year ending March, 1938, and earlier volumes.

TABLE D-I

Standard Objects of Expenditure

Object No.	Description
(1)	Civil Salaries and Wages
(2)	Civilian Allowances
(3)	Pay and Allowances - Defence Forces and R.C.M.P.
(4)	Professional and Special Services
(5)	Travelling and Removal Expenses
(6)	Freight, Express, and Cartage
(7)	Postage
(8)	Telephones, Telegrams and Other Communication Services
(9)	Publication of Departmental Reports and Other Material
(10)	Exhibits, Advertising, Films, Broadcasting and Displays
(11)	Office Stationery, Supplies, Equipment and Furnishings
(12)	Materials and Supplies
(13)	Construction or Acquisition of Buildings and Works including Acquisition of Land
(14)	Repairs and Upkeep of Buildings and Works
(15)	Rental of Buildings, Works and Land
(16)	Construction or Acquisition of Equipment
(17)	Repairs and Upkeep of Equipment
(18)	Rental Equipment
(19)	Municipal or Public Utility Services
(20)	Contributions, Grants, Subsidies, etc. not included elsewhere
(21)	Pensions, Superannuation, and Other Benefits in Consideration of Personal Services
(22)	All other Expenditures (Other than Special Categories)

TABLE D-I -- ConcludedSpecial Categories

Object No.	Description
(23)	Interest on Public Debt and Other Debt Charges
(24)	Subsidies and Special Payments to the Provinces
(25)	Family Allowances Payments
(26)	Old Age Pensions, Allowances to the Blind and Disabled and Unemployment Assistance
(27)	Veterans' Disability Pensions and Other Payments under the Pension Act
(28)	Other Payments to Veterans and Dependents
(29)	Government's Contribution to the Unemployment Insurance Fund
(30)	Hospital Insurance and General Health Grants
(31)	Trans-Canada Highway Contributions
(32)	Movement of Mail by Land, Air and Water (Post Office)
(33)	Deficits - Government Owned Enterprises

establish a departmental classification under which were grouped expenditures relating to the services and operations for which the departments were responsible. In a statement regarding this revision in the form of the estimates, the then Minister of Finance, C.A. Dunning, pointed out that the purpose of the revision was to

. . .facilitate a greater control over expenditures and to present a clearer and truer picture of the operations of government. . . [and] . . .to give to parliament. . . a reasonably accurate estimate of the costs of functions, assembled under the departments responsible for administration.³⁹

An item was inserted for each distinct service or operation while other expenses which could not be allocated on this basis were included under an item for administration of the department.⁴⁰ Each item was given a vote or appropriation number.

The new form of Estimates introduced in 1938 was composed of two main sections. The first was made up of items representing operations and services and was to be included in the supply bill. The second section, designed to furnish Parliament with further information, consisted of the breakdown of the items in the first section into objects of expenditure such as types of personnel employed, supplies, travelling expenses, etc. These objects did not follow a prescribed, uniform classification such as the standard objects of expenditure classification presently in effect.

Basically the form of the estimates has not changed since 1938 although certain revisions have been made to simplify and clarify the estimates. In 1950 the standard objects classification was developed to establish a degree of uniformity in the detailed section of the estimates relating to the materials purchased. It also served to provide

³⁹Debates, February 3, 1938, p. 148.

⁴⁰For instance, in the Department of Agriculture, expenditures would be classified under such items as follows:

No. of Vote	Marketing Services
6	Marketing Services Administration
7	Agricultural Economics
8	Dairy Products
9	Subsidies of Cold Storage Warehouses
11	Livestock and Poultry
	Production Services
13	Production Services Administration
	Health of Animals
14	Administration of Animal Contagious Diseases Act
15	Compensation for animals slaughtered
16	Livestock and Poultry

information for the executive and Parliament regarding the total amount spent by the government on any one particular object, (e.g. advertising, rentals, etc.).⁴¹ Since 1961 other changes in the form of the estimates have followed. Beginning with the 1964-65 estimates, a revised vote or appropriation pattern was adopted in which various appropriations which had previously been shown separately were consolidated. The result has been a reduction in the number of votes in the main estimates from approximately 500 to 250.⁴² Furthermore, this was accomplished in such a way as to preserve the amount of information in the details section so that there would be no loss of information available to Parliament. A consequence of this recent change, as will be discussed shortly, will be to lessen the degree of control that Parliament exercises over expenditures.

The form of the first or vote section of Estimates is illustrated in Part I of Table D-II with a sample from the expenditure estimates of the Department of Transport. It will be noted that the expenditures of the department are presented in the form of estimates for the various major services of the department such as Marine Services, Railways and Steamships, etc. The expenditures relating to these services are grouped into categories indicating the nature of the expenditures and each is assigned a vote number. The categories illustrated, "Administration", "Administration, Operation and Maintenance", and "Construction or Acquisition of Buildings, Works, Land and Equipment", are the principal ones found throughout the estimates, and, as further illustrated, usually include a very brief description.

Part II is an illustration of the form in which the details section of Estimates is presented in respect to the operating and capital votes. The expenditure provided for by each vote is divided among the various sub-divisions of the service to which it relates. For instance, expenditures for the administration, operation, and maintenance of Marine Services are distributed among such sub-divisions as Marine Services Administration, Aids to Navigation, Canals, etc. Where these sub-divisions involve capital expenditures, they are provided for separately by the capital vote. The objects of expenditure pertaining to each sub-division are also presented.

Determination of Expenditure Estimates Within Departments

The process of preparing expenditure estimates varies from

⁴¹This question was raised in the Public Accounts Committee in 1950. Members of the Committee believed that such information would be of interest to parliament. See Canada, House of Commons, Standing Committee On Public Accounts, Minutes of Proceedings and Evidence, May 4, 1950, pp. 201-206.

⁴²In 1962-63 the total number of votes, excluding supplementary votes, was roughly 495.

TABLE D-II

EXPENDITURE ESTIMATES

TRANSPORT

PART I

Present Form of Vote Section - Main Estimates

No. of Vote	Service	1964-65 \$	1963-64 \$	Change	
				Increase \$	Decrease \$
A - Department					
S	Minister of Transport - Salary and Motor Car Allowance (Details, p. 455)	17,000	17,000		
1	Departmental Administration (Details, p. 455)	3,773,800	3,605,600	168,200	
Marine Services					
5	Administration, Operation and Maintenance including fees for membership in the international organizations listed in the details of the Estimates, pensions, grants and contributions as detailed in the Estimates, the payment of expenses incurred in res- pect of Canadian distressed seamen as defined in section 306 of the Canada Shipping Act and, in respect of the Canadian Coast Guard Ser- vice, authority to make recoverable advances for transportation, steve dor- ing and other shipping ser- vices performed on behalf of individuals, outside ag- encies, and other govern- ments and authority. . . (Details, p. 957)	38,249,400	37,547,600	701,740	

TABLE D-II -- Continued

No. of Vote	Service	1964-65	1963-64	Change	
				Increase	Decrease
10	Construction or Acquisition of Buildings, Works Land, Vessels and Equipment including payments to Provinces or Municipalities as contributions towards construction done by those bodies (Details, p. 466)	31,942,000	24,390,900	7,551,100	
		70,191,400	61,938,560	8,252,840	

PART II

Present Form of Details Section - Main Estimates

Positions (man-years)		Details of Services	Amount	
1964-65	1963-64		1964-65	1963-64

A - Department

Marine Services

Vote 5 - Administration,
Operation and Maintenance
including fees for membership
in the international
organizations. . . .

Marine Services Administration,
Including Agencies

Salaried Positions:

Administrative and Professional:

1	1	Senior Officer 3 (\$17,400 - \$19,000)
1	1	Senior Officer 1 (\$14,800 - \$15,800)
6	2	(\$10,000 - \$12,000)
4	8	(\$ 8,000 - \$12,000)
26	26	(\$ 6,000 - \$ 8,000)

TABLE D-II -- Continued

Positions (man-years)		Details of Services	Amount	
1964-65	1963-64		1964-65	1963-64
		Technical, Operational and Service:		
1		(\$10,000 - \$12,000)		
1	1	(\$ 8,000 - \$10,000)		
6	5	(\$ 6,000 - \$ 8,000)		
33	30	(\$ 4,000 - \$ 6,000)		
34	34	(Under \$4,000)		
		Clerical		
69	75	(\$ 4,000 - \$ 6,000)		
67	67	(Under \$4,000)		
2	2	(Part Time)		
<hr/> 251	<hr/> 252			
(250)	(251)	Continuing Establishment	1,116,900	1,083,635
<u>(1)</u>	<u>(1)</u>	Casual and Others-----	<u>2,700</u>	<u>2,700</u>
(251)	(252)	Salaries and Wages-----	1,119,600	1,086,335
		Overtime----- (1)	6,000	6,000
		Allowances----- (2)	1,800	1,800
		Travelling and Removal Expenses----- (5)	22,400	21,850
		Freight, Express, and Cartage----- (6)	1,300	1,325
		Postage----- (7)	7,000	6,600
		Telephones and Telegrams (8)	22,600	22,600
		Office Stationery, Sup- plies and Equipment- (11)	16,200	16,150
		Materials and Supplies- (12)	4,700	4,750
		Municipal or Public Utility Services---- (19)	2,100	2,125
		Sundries----- (22)	<u>1,000</u>	<u>1,000</u>
			<u>1,204,700</u>	<u>1,170,535</u>

TABLE D-II -- Continued

Positions (man-years)		Details of Services	Amount	
1964-65	1963-64		1964-65	1963-64
<hr/>				
		Expenditure		
		1961-62	\$1,065,986	
		1962-63	1,143,334	
		1963-64	1,183,354	
		(Estimated)		
Vote 10 - Construction or Acquisition of Build- ings, Works, Land, Ves- sels and Equipment				
Aids to Navigation- Construction or Acqui- sition of Buildings, Works, Land and Equip- ment				
Construction or Acqui- sition of Buildings, Works and Land----- (13)				
			4,417,000	5,846,850
Construction or Acqui- sition of Equipment- (16)				
			723,000	821,550
			5,140,000	6,668,400
Less Anticipated Fees			855,000	748,400
			<u>4,285,000</u>	<u>5,920,000</u>
<hr/>				
		Expenditure		
		1961-62	\$4,513,007	
		1962-63	4,298,851	
		1963-64	4,850,000	
		(Estimated)		
St. Lawrence and Sagu- enay Rivers Ship Channels- Construction or Acquisi- tion of Buildings, Works, Land and Equipment				
Contract Dredging - St. Lawrence Ship Channel				
			3,812,000	3,230,000
Contract Dredging - Saguenay River				
			50,000	50,000
Construction or Acquisi- tion of Buildings, Works, and Land				
			108,000	
		(13)	<u>3,970,000</u>	<u>3,280,000</u>

TABLE D-II -- Concluded

Positions (man-years)		Details of Service	Amount	
1964-65	1963-64		1964-65	1963-64
<hr/>				
		Expenditure		
		1961-62	\$4,457,584	
		1962-63	3,250,000	
		1963-64	6,030,000	
		(Estimated)		

Source: Canada, Estimates for the Fiscal Year ending March 31, 1965, pp. 450-451, 457, 466.

department to department. Consider the Department of Transport as an example. Directives regarding estimates submission are issued by the Treasury Board to the Financial Services Division of the department. This division interprets the directives to the operating divisions of the department through the Deputy Minister. The estimates are prepared by division heads. The standard or guide used has generally been the expenditure of the past fiscal year. The operating services generally submit their estimates to the Deputy Minister for preliminary review in a piecemeal fashion as they are prepared by departmental branches. After adjustments are made as suggested by the Deputy Minister, the individual branch submissions are forwarded to the Financial Services Division where they are co-ordinated and consolidated into one complete estimates submission.

The Department of Northern Affairs and National Resources generally begins the preparation of estimates in May for the coming fiscal year. The estimates are prepared in three phases, namely, capital, operation and maintenance, and establishment. The estimates for capital projects are prepared in the field as a work program for the subsequent two years. They are submitted to headquarters branch directors as "planned estimates." Upon review by the branch directors and upon approval of the projects, they are communicated back to the field and form the basis for the submission of the main estimates. There does not appear to be very much co-ordination in compiling the estimates in the three categories mentioned above. The result may be the construction of a project but no personnel provided in the estimates for its operation and maintenance.

In general, the estimates are prepared on the basis of what a department might expect to receive. An estimates review is conducted at the Branch level, at the Deputy Minister level, and at the Ministerial level within a department. Reductions are generally made in the process of each of these reviews, but the basis of the reductions is questionable. It is difficult to determine the criteria used to make these reductions. It appears to be fairly arbitrary with no planned pattern other than the concept that an overall reduction in a department must be effected in accordance with the Treasury Board directive. Invariably the reductions

are made on the basis of the standard objects and are of such general nature that they cannot be related to a specific project within an operating area. In the Northern Administration Branch of the Department of Northern Affairs and National Resources it appears that reductions are arbitrarily apportioned to districts.

Departmental expenditure planning as part of the administrative process has been almost negligible within most government departments in the past. Following the Glassco Commission investigation and report, departments began to place emphasis on the planning function but, in general, both short-term and long-range financial planning is still rather weak. Where planning has been established, the quality of the supporting statistical and financial data has generally been poor. Planning among departments, and even among branches within a department, varies and no formalization of the planning process has been established.

Increasing emphasis, however, is presently being placed on departmental planning. The Marine Services Branch of the Department of Transport has developed plans on a ten year basis covering most of the major capital expenditures of each of its divisions. For instance, plans have been made for the construction of ships involving the replacement and expansion of the Coast Guard fleet for 1964-70. This plan is reflected in a document which is updated from time to time and is submitted to the Treasury Board for review in order to obtain approval in principle for the proposed undertaking.

In the Air Services Branch of the Department of Transport, planning on the basis of detailed five year requirements is beginning to reach a certain degree of sophistication. The planning is undertaken on a regional basis. Table D-III is a sample of the details now presented for what is termed a five year capital program (1964-69) for the Moncton Region as prepared in May, 1964. Part I shows the details as they are prepared in site summary form. Part II consists of an example of the form in which justifications for the 1965-66 expenditure items are prepared.

A very recent development in Air Services is the preparation made to adjust the estimates during the fiscal year should the Treasury Board direct such an adjustment on short notice. Regions have been requested to include a list of projects from the 1965-66 capital estimates which might be deferred. This list is to represent one third of the votes, and items are to be listed in order of declining priority. A list of items from the 1966-67 program is also to be provided covering 10 percent of that program which could be advanced into 1965-66.

The Form of Departmental Expenditure Submissions to Treasury Board

The form of the estimates as they are prepared by the departments and agencies for submission to the Treasury Board staff follows the pattern of the Estimates Blue Book, except that the estimates include more detail in this earlier stage of the process. This detail includes a general description of the function of each division of the department and the services it is providing, as well as details regarding objects purchased.

TABLE D-III -- Concluded

PART II

PROGRAM ITEM AND SITE: 5-027-013 - Strengthen 1500' of R/W 07-25
SYDNEY AIRPORT, N.S.

Facts Which Demonstrate the Need for the Project as submitted by AIRPORTS & PROPERTY MANAGEMENT DIVISION:

The main portion of this runway is in good condition; 1500' of the 07 end was sandsealed during the summer of 1963 over the original construction of 1949 and this area is deteriorating and showing signs of traffic stress. The heavy Vanguard aircraft now using Sydney Airport is causing a more rapid breakup; cracking and rutting is prevalent, therefore, it will require major maintenance if the trend stands. We recommend that this portion only of the runway be strengthened to carry the loading of the heavier aircraft.

Strengthen and recap 1500' x 200'.

1965-66

Capital (\$'000)

Installation 55.

Contingencies 5.

Supervision 5.

Maintenance 65.

Source: Department of Transport, "Five Year Program (1964-69), Main Estimates 1964-65", (Unpublished).

The objects of expenditure, as they are prepared by the departments, follow the prescribed standard objects classification, accompanied by an explanation of the objects and by explanations of any increase or decrease in the amount as compared to the previous year. The amount of detail included varies from department to department with some departments presenting more detailed explanations of their estimates than others. Expenditures of a capital nature, such as those of the Department of Public Works, are generally explained more fully.

Typical of the type of information contained in the estimates prepared and submitted by departments are the estimates of the Department of Transport. The service "Aids to Navigation - Administration, Operation and Maintenance" is explained generally as consisting of the administration and operation of lighthouses, fog alarms, buoys, beacons, etc., surveying and acquiring lighthouse sites, publications, issuing notices to Mariners, and removal of wrecks which are obstacles to navigation. The construction

aspect of this service is explained in similar terms, that is, as providing for new construction of lighthouses, light-keepers dwellings, fog alarm buildings, piers, etc. The amount spent in various geographical areas is usually indicated. For certain services undertaken by the department, such as airports and ground services, the number of personnel directly employed may be given on a regional basis. In some cases, such as Vote 10 in Table D-II, "St. Lawrence and Saguenay River Ship Channels", the type of construction work that is planned may be spelled out in certain detail, and a brief statement regarding the general purpose of this work may be included. In few of the departmental submissions does the description of a service or a construction project contain an objective justification of the expenditure proposed. Certain submissions may approach an objective justification, for example, an expenditure of the type providing for the construction of harbour facilities. The Department of Public Works, in relation to its harbours and rivers engineering services, may propose to re-construct a wharf or provide a breakwater extension in a specified area. The estimates submission may describe the project, including information concerning the geography of the area, the proximity of other similar facilities, the occupations of the people of the area and the number of people and boats served. For instance, should it serve mainly fishermen, a statement may be included regarding the value of the previous year's fishing catch. Such informative detail is generally the exception rather than the rule. In most cases where a department provides a continuing service, little or no indication is given as to whether the service is actually a continuing necessity. For new proposed services or construction projects information is seldom contained, if at all, in the formal departmental estimates submissions regarding the expected benefits of the service or project as opposed to the costs, which might justify its provision.

The present content of the estimates submissions is largely uninformative in communicating information that would appear to be useful to Treasury Board in its review process.⁴³ The explanations and justifications accompanying the estimates as submitted to Treasury Board are largely rewrites of those given in previous years. The Treasury Board, striving for uniformity and consistency in presentation, generally receives uniform and consistent explanations for widely differing operating activities. Departments consequently do not justify their estimates in the most meaningful manner that they are capable of in view of the information that the departments

⁴³The Glassco Commission has been very critical of the form and content of the estimates: "The form of the Estimates does not permit intelligent criticism and, in placing the major emphasis on the nature of expenditure rather than on its real purpose the matters coming under senior review are the less important details of administrative judgment. Any valid assessment of performance by departmental management is excluded, and it is virtually impossible to form any objective judgment from the Estimates as to the desirability of continuing, modifying, or enlarging specific programs in the public interest". Canada, The Royal Commission On Government Organization (Ottawa: Queen's Printer, 1962), Vol. I, p. 100.

have at their disposal.

Since 1962 the departments have been required to include three-year forecasts of expenditures in their annual submission of estimates to the Treasury Board. The forecast is required to be submitted in two parts as follows:

Part I - A departmental summary consisting of departmental totals for the current year and the next three years, subdivided into three categories:

- (i) Administrative votes - all standard objects other than those included in (ii) and (iii).
- (ii) Capital votes - standard objects numbered (13) and (16).
- (iii) Grants, Subsidies, and other votes - standard objects numbered (20) and (23) to (33).⁴⁴

Part II - Supporting details for each of (i), (ii) and (iii) in Part I to consist of expenditures for "current" and "new" programs.⁴⁵

The form in which the forecast material is presented is illustrated in Tables D-IV and D-V representing Parts I and II (ii) respectively. "Current" programs are defined as those currently approved whereas "new" programs are those which are proposed but have yet to receive approval. For instance, a proposal to extend a certain service into new areas would represent an increased level of service requiring a Cabinet or Treasury Board decision, and the cost involved would be reflected under a "new" program for the year, or accumulatively over the years. The estimated amounts are based on existing price levels although the details section pertaining to administrative votes allows for increases in salaries over the forecast period.

Treasury Board Review

As was mentioned earlier, the Treasury Board is a committee of the Privy Council composed of the President of the Privy Council, named to be President of the Board, and five other Cabinet ministers, and is served by a secretariat under the direction of an officer named to be Secretary of the Board. The Treasury Board secretariat is divided into various units bearing responsibility for such financial matters as expenditure program analysis, for advising on matters of personnel policy, and for establishing procedures in financial administration. Various changes have recently been made in the organization of the secretariat.

The present organization of the secretariat is illustrated in the adjoining chart where it will be noticed that the secretariat is divided

⁴⁴See Table D-I, the standard objects and special categories classification.

⁴⁵See Canada, Department of Finance, Estimates Manual (Ottawa: Queen's Printer, 1956. Including amendments to 1965).

TABLE D-IV

FORECAST OF ESTIMATES - DEPARTMENTAL SUMMARY

Department of Transport

	19(C.Y.)	19(N.Y.)	19(N.Y.+1)	19(N.Y.+2)
	<u>Current</u>	<u>NEW</u>	<u>Total</u>	<u>C. N. T.</u>
Administrative Votes				
1 Departmental Administration				
5 Marine Services Administration				
- - - - -				
Capital Votes				
10 Marine Services Construction				
40 Civil Aviation Construction				
- - - - -				
Grants, Subsidies, etc.				
45 Contributions for Airport Development				
- - - - -				
Total Department				

Source: Canada, Department of Finance, Estimates Manual.

TABLE D-V

FORECAST OF ESTIMATES - DETAILED CAPITAL VOTES

Department of Transport

Vote 40 - Civil Aviation: Construction or Acquisition of Buildings, Land and Equipment.

19(C.Y.) 19(N.Y.) 19(N.Y.+1) 19(N.Y.+2)

Approved Projects
(in progress)

(1) Gander - (Project,
e.g. reconstruction
of runway)

(2) Montreal - (Project,
e.g. terminal building)
(not yet started)

(1) Halifax - (Project)

Total "Current"

Projects Not Yet Approved

Quebec (Project)

Ottawa (Project)

Total "New"

Vote Total

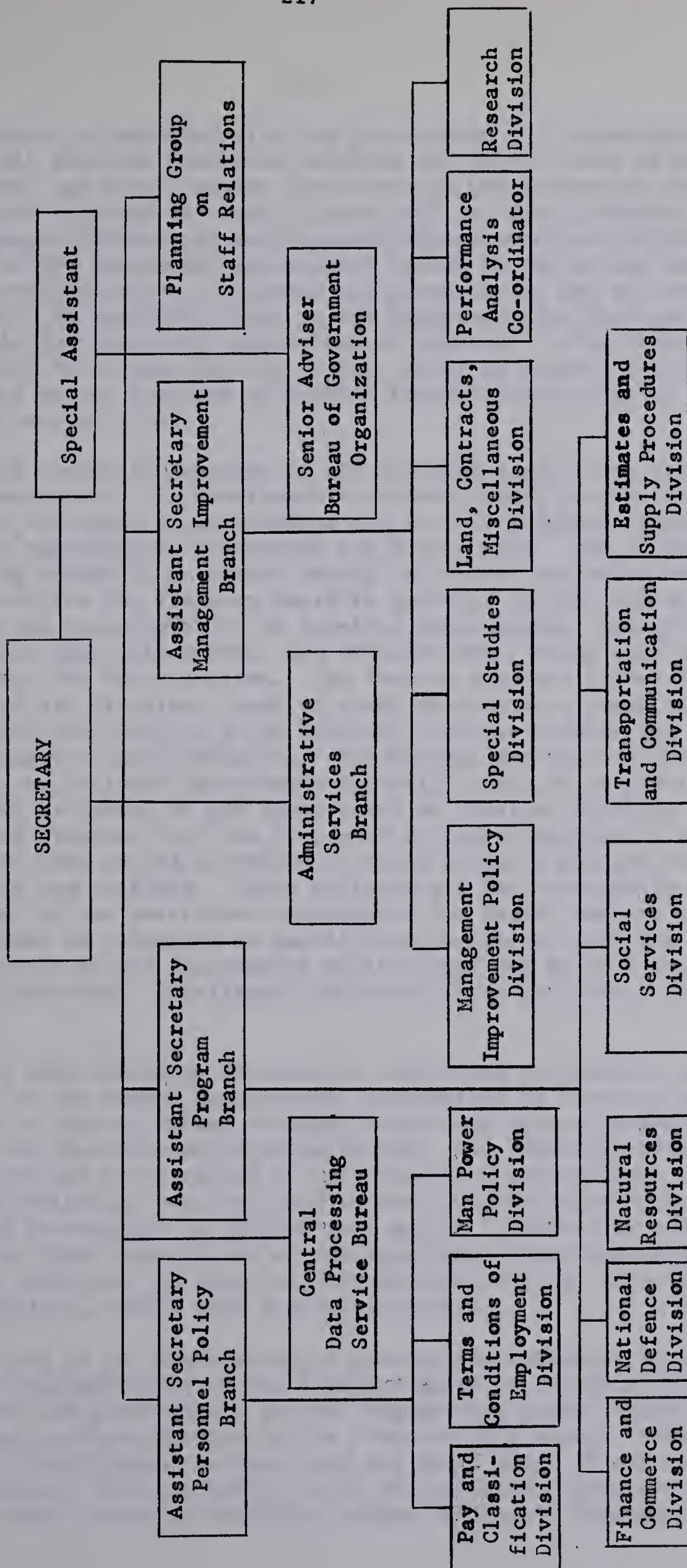
Source: Canada, Department of Finance, Estimates Manual

into three main branches, each under the direction of an Assistant Secretary to the Board and composed of various sub-units, and three subordinate divisions. The Program Analysis Branch is responsible for the examination of the expenditure proposals and programs of the various departments and agencies as they are presented for approval to the Board at estimates time and throughout the course of the year. The Personnel

TABLE D-VI

TREASURY BOARD SECRETARIAT

ORGANIZATION CHART

Source: Treasury Board Organization and Administration Manual, (March, 1965)

Policy Branch is concerned with the preparation and presentation to the Board of all material regarding salaries and wages, hours of work, manpower utilization, and other working conditions in the government service. In this respect it works in close liaison with the Civil Service Commission which forwards information and recommendations on these problems. The function of the Management Improvement Branch is to develop and recommend improved administrative procedures and practices in the departments of government. In addition, there is the Administrative Services Branch, responsible for providing administration services to the Board, and the Central Data Processing Service Bureau, which is responsible for informing departments of the location of machine installations in other departments and their availability.

The essential function of the Treasury Board is to allocate the scarce resources at the government's disposal among the various competing government departments and agencies and to make judgments regarding government expenditures throughout the fiscal year. The allocation function is primarily performed during the annual estimates review, and in this function the Treasury Board is assisted by the Program Analysis Branch of the Secretariat which receives departmental expenditure submissions, scrutinizes them, and forwards them, along with recommendations, to the Board for consideration. The Program Analysis Branch is presently composed of six divisions, each of which deals with a group of departments and agencies performing a given function, such as finance and commerce, natural resource development, etc. The Program Analysis officers in these divisions are assigned departments for which they are responsible. The expenditure estimates or any submissions or problems relating to expenditure programs that are presented by those departments to Treasury Board first come to the attention of these officers who conduct an examination and analysis. These officers are not necessarily experts in the work of the particular departments for which they are responsible, although they do endeavour to familiarize themselves with the organization and objectives of the departments so that they may be in a position to conduct a reasonably intelligent review of their policies and expenditure programs.

In many instances substantial supporting information is not contained in the formal departmental submissions to Treasury Board but is bridged to a certain extent through discussions between program analysis officers and departmental representatives. The treasury officer is in constant contact by telephone or otherwise with key officers of the department which has been assigned to him. On the other hand, further supporting information in written form may be requested by treasury officers in their examination of any particular departmental expenditure proposal. Officers, on occasion, may conduct on-site inspections of a capital project, should they deem it desirable.

Prior to the submissions of expenditure estimates by departments, it is the responsibility of the Treasury Board to interpret to the departments the government's general expenditure policy objectives for the ensuing year as conveyed by the Minister of Finance. These objectives influence the attitude the Board and its staff adopt in the expenditure review process. On this matter, G.E. Steele, former Secretary of the Treasury Board, recently testified before the Senate Standing Committee

on Finance as follows:

...it is usual for the Minister of Finance to have discussed with his senior officials in a tentative way the sort of budgetary problem he envisages for the ensuing year. If serious difficulties are foreseen which require a particular attitude to be adopted in the estimates review, then this viewpoint is communicated immediately to departments, sometimes in writing, sometimes by means of top level exchange between Treasury and departmental staff. For example, I have noted that since it is the stated view of the Government at the present time that the Minister of Finance will strive to achieve a smaller net deficit position between revenue and expenditures, it is vital that departments discuss the phasing of their plans so as to avoid what we call a peaking up of the expenditures particularly at this time.⁴⁶

Steele explained that, in attempting to reduce the budgetary deficit situation, the Treasury Board "has been pretty ruthless in new spending programs, and at the time of the review last year there were some considerable cut-backs It is not at all unusual in estimates for the Treasury Board operation to result in a reduction of \$100 million from the submissions put up by a department."⁴⁷

Departments are encouraged to obtain Cabinet approval in principle of policy and major expenditure proposals prior to the inclusion of these proposals in the annual estimates submissions, and one aspect of the Treasury Board examination of the estimates is from this point of view. That is, the expenditure estimates are required to be submitted for approved programs only, and it is the function of Program Analysis officers to examine the estimates to ascertain whether this is in fact the case. In the words of G.F. Davidson, Secretary of the Treasury Board,

...plans are examined...by the Treasury Board staff who will ask a variety of questions as to whether cabinet authority for certain particular items included has been obtained, or whether this particular project and that expenditure program should be included in the estimates.⁴⁸

It is necessary, however, to preserve a sense of proportion in this matter, for a small change in the nature of a service may not merit the attention of the whole Cabinet. Normally the Treasury Board will deal with the minor items amounting to \$5,000 or \$10,000 in the estimates which provide for such changes. For anything of real substance, however, the Board will request that the Cabinet clear the policy before considering it for approval. All in all, it is obviously necessary that the Treasury Board staff be thoroughly familiar with the departmental policies that

⁴⁶The Senate of Canada, Proceedings of the Standing Committee on Finance, May 26, 1964, p. 9.

⁴⁷Ibid., p. 13.

⁴⁸Ibid., Oct. 13, 1964, p. 137.

have been enunciated if they are to make judgments as to whether or not expenditure proposals come within these policies. As one director of the Program Analysis Division has stated,

...not only should individual proposals conform with the policy that has been declared but also policy that has not been declared. Policy of course is not always explicit in its details and the staff member should be able to recognize if proposals are consistent or not, or even if the acceptance of the proposals would in effect establish a policy without the full and proper consideration of all the implications by the Cabinet.⁴⁹

In general, new program proposals by departments are subjected to a more thorough review by program analysis officers than are established programs of a continuing nature. There is a tendency to focus attention on the proposed increments of continuing programs rather than to undertake an examination of the entire program. This process has been fittingly described by the Secretary of the Treasury Board:

I think it is quite fair to say, for example, that in the present estimates process...an abnormal amount of time is spent on justifying the additional numbers of people that you require and the additional amounts of money that you require, while a relatively small amount of time is spent each year in justifying all over again the people you already have and the dollar amounts that you already have been accustomed to using in the departments.

What this means is that...you are concentrating all your attention on the 10 percent, perhaps, of new bodies that a department wants to employ, and on the 10 percent of new dollars that are asked for; and you are not asking questions that you should be asking about the 90 percent of the program costs which represent the people that you have already had on staff for years, and the programs that have been carried on more or less automatically for some considerable time.⁵⁰

The cost analysis is conducted with a view to determine whether the amount of funds specified in the estimates for the various services and activities are reasonable and whether economies can be achieved in any particular areas. The Treasury Board staff or secretariat examines each expenditure item to determine, in effect, whether the department concerned can get by on less. Estimates are reduced in cases where the secretariat judges that certain sums are unnecessary, or where the secretariat finds inadequate justification for including certain items in the estimates. Meetings between the staff of a particular department and program analysis officers in Treasury Board generally result in a

⁴⁹ T.H. Bennett, "The Treasury Board and the Defence Budget," The Treasury Board, Four Talks Delivered in a Seminar by the School of Administration, Carleton University, Ottawa, January 28, 1960, (Unpublished) p. 7.

⁵⁰ Senate of Canada, Proceedings of the Standing Committee on Finance, Tuesday, Oct. 20, 1964, p. 167.

substantial reduction in overall expenditures. It should be noted, however, that the Treasury Board secretariat does not possess the power to reject or reduce an expenditure unless the department concerned agrees to the reduction. Where such an agreement is not reached, the decision is left to the Treasury Board. Treasury Board officers can nevertheless exercise considerable influence over Treasury Board decisions by the information and recommendations they supply. The expenditure estimates material is prepared by the secretariat for submission to the Treasury Board, and included in this material are recommendations and supplementary information regarding any questionable expenditure proposals or areas of disagreement between the secretariat and the departments. The Secretary of the Treasury Board has recently described this procedure as follows:

We do not take the responsibility at the staff level of making the reduction unless the deputy minister himself agrees to our doing so. If we cannot reach agreement with the deputy minister on a smaller sum that we can recommend, or if we are not ourselves convinced that the sum is required and can be approved in principle for this purpose, we will put a recommendation to the Treasury Board stating that in our judgment the full amount requested is not required and that a lesser amount will suffice for the purpose. The Treasury Board must then take the position that they are or are not prepared to go beyond a certain amount.⁵¹

If a department is not willing to accept the decision of the Board in regard to its expenditures the department may appeal to the Cabinet.

At the present time, with the recent requirement that departments include three-year forecasts of their expenditures in their annual submission of estimates, Treasury Board officers must not only be concerned with reviewing departmental estimates for the coming fiscal year but also beyond this period. Prior to this introduction of forecasting, the Treasury Board did look to future year commitments in some areas such as National Defence, but in most other areas this was not done. The establishment of forecasting has been a significant step in the expenditure review process, for it causes both departments and Treasury Board to consider the financial implications for the future of the programs and projects which they recommend today.

In considering the process of Treasury Board review of departmental expenditure plans and programs, particularly those of a capital nature, a distinction should be made between an examination of these programs in terms of their financial and policy implications and an examination in purely technical terms, the latter requiring engineering personnel and technicians. Referring to construction projects which are highly technical in nature, the Secretary of the Treasury Board, G.F. Davidson, in a recent appearance before the Senate Committee on Finance, stated:

...the Treasury Board does not have its architects and engineers, and does not attempt to impose its technical views in those areas on the technical advice that the departments are either in a position to provide for themselves through their own personnel, or the technical consultants which they have obtained from outside. I think the basic

⁵¹The Senate of Canada, Proceedings, October 13, 1964, p. 137.

position the Treasury Board must inevitably take in all these construction proposals is that it must satisfy itself the department undertaking the construction is operating on the basis of competent technical advice. . . . the Treasury Board has the responsibility, before it approves a construction program put forward by any department, to satisfy itself the proposal has been examined and found to be sound on the basis of the best and most competent technical advice that can be found inside or outside the government service. If there were a project being put forward by an individual department where it was clear the Public Works Department had more competent technical experts to examine that particular project, I think clearly Treasury Board would wish to have the advice of the Department of Public Works.⁵²

The Board does not consult technicians from outside the public service directly, but it does insist from time to time that the departments do so and that the advice given by the technicians be provided to the Board through the departments.⁵³ Consequently, while the Treasury Board is not primarily concerned with a purely technical review of capital projects, the technical aspects of the projects are not dismissed altogether. In general, however, the Board is more concerned with the manner in which such projects fit into departmental policies and over-all program plans than with the technical aspects.

One of the main difficulties confronting the Treasury Board and its staff is the absence of a market test of efficiency or profitability by which departmental programs may be measured. In a sense the function of the Treasury Board, in the expenditure review process, is to act in lieu of the price system in the market economy. Treasury Board analysts therefore require some objective standards or criteria as a basis on which expenditure proposals may be examined and evaluated in terms of the quality of goods and services provided and the efficiency of operation, together with a view to establishing priorities among the proposed programs. Without such standards the estimates review procedure would consist of a single exercise in judgment and a conflict of opinion where differences between program analysts and departmental officials arise. The Treasury Board secretariat has attempted to reduce expenditure proposals to some measurable basis by developing certain standards to be applied to various areas, for instance, standards to be applied to the construction of government buildings and for the purchase of equipment. With regard to the development of standards, one Director in the Program Analysis Division has stated:

...considerable progress can and will undoubtedly continue to be made. It is relatively simple to apply known costing techniques to such things as salary requirements. Normal repairs and maintenance for

⁵²Ibid., June 9, 1964, p. 71-72.

⁵³Ibid., p. 72.

many types of equipment such as vehicles can be determined by applying attrition rates common in industry. Similarly capitation rates have been developed in industry for such things as food consumption or requirements for medicine, clothing, etc. In addition the cost of new construction can be reduced to so much per square foot for certain types of construction. It should be remembered that such rates or standards are at best a guide and the staff officer must constantly assess the validity of claims that, for this or that reason, the standard norm cannot apply.⁵⁴

In the case of rentals paid on buildings there is an examination by Treasury Board into the prevailing rental in the particular area in question and this is applied as criterion. If the leasing proposed is X dollars per foot, Treasury Board requires that it be informed whether that is high, low, or normal in that particular area. The Treasury Board has requested and encouraged departments to develop adequate criteria by which the various types of programs which appropriately lend themselves to such analysis may be evaluated.

The fact that the main expenditure estimates are considered by the Treasury Board and its secretariat in a relatively short period of time places considerable pressure on the Board during what is known as estimates time. The secretariat reviews the estimates during a five or six week period in October and November, and the ministers of the Board meet for approximately three weeks in the early part of December. It is therefore indeed difficult for the ministers to go into very much detail in the case of each department. Rather, they generally concern themselves with the relation of programs to policy and to the general objective of the budget. It is during these deliberations that priorities are established among programs, and frequently there is a considerable reduction in the estimates of individual departments as programs judged to be of lesser priority are either cancelled or postponed. Any differences concerning the estimates of a particular department between the department and the Treasury Board secretariat are resolved at this time. After hearing representations from the Minister of the Department concerned and his officials and after hearing the representatives of the secretariat, the ministers pass judgment on the programs or projects in question.

Parliamentary Review

Committee of Supply

The formal procedure by which departmental expenditure estimates are received and authorized by Parliament has already been outlined briefly.

⁵⁴T.H. Bennett, "The Treasury Board and the Defence Budget," The Treasury Board, Four Talks Delivered in a Seminar Arranged by the School of Administration, Carleton University, Ottawa, on January 28, 1960, (Unpublished), p. 6.

It was pointed out that the House of Commons considers the estimates in Committee of Supply and the estimates are introduced for the individual departments by the Ministers concerned. The Committee then conducts a vote by vote examination of the estimates.

The manner in which these spending estimates are consolidated into votes or appropriations is of considerable significance, for it is only the vote section of the estimates that is included in the Appropriation Bill and consequently only the vote description has legislative effect and is binding on the administration. The details of the estimates are presented for the information of Parliament although they are also binding to a limited degree. On this matter the Financial Administration Act specifies that:

At the commencement of each fiscal year or at such other times as the Treasury Board may direct, the deputy head or other officer charged with the administration of a service for which there is an appropriation by Parliament or an item included in the estimates then before the House of Commons, shall prepare and submit to the Treasury Board through the Comptroller, a division of such an appropriation or item into allotments in the form detailed in the estimates submitted to Parliament for such appropriation or item, or in such other form as the Board may prescribe, and when approved by the Board the allotments shall not be varied or amended without the approval of the Board, and the expenditures charged to the appropriation shall be limited to the amounts of such allotments.⁵⁵

In accordance with this specification a department may submit to Treasury Board an alternative breakdown of the vote, perhaps by programs, projects, or regional offices, rather than by the standard objects shown in the detailed estimates. On Treasury Board approval funds may be transferred from one such allotment to another. This is generally a routine Treasury Board decision. Under no circumstances, however, may funds be transferred between votes.

It is therefore quite apparent that the recent re-grouping and consolidation of the estimates will have an effect on the degree of control of expenditures that Parliament exercises. Consider, for example, Vote 5 of the Department of Transport which provides for the administration, operation, and maintenance of Marine Services. By consolidating under this vote the administration of aids to navigation, canals, St. Lawrence and Saguenay River Ship Channels, the Canadian Coast Guard, and Marine regulations, it is true that there is less detail for the House to go through in the appropriation section, but it also means that the government is left with a greater opportunity to shift manpower and funds from one object to another or from one purpose to another and in such decisions Parliament is not consulted. This may be desirable, for, as government operations increase, Parliament is left with less and less time for preoccupation with the individual details of expenditure. Parliament could very well make more profitable use of its

⁵⁵ Statutes, 15-16 Geo. VI, c.12, s.29.

time by dispensing with these details and focusing attention on the overall purposes and objectives of expenditures appropriately presented in the form of meaningful programs.

The presentation of the estimates of a department before the House provides an opportunity for Parliament to discuss departmental policies and the role of the federal government in its various fields of activity. This presentation generally follows a pattern. The Minister of the Department concerned makes an introductory statement in which he outlines briefly the functions and policies of his department, describes any special proposals initiated for the fiscal year, and comments on the amounts being spent in various areas and on increases or decreases in spending in such areas. This outline of department policies in the introduction is desirable in the sense that the members of the House may subsequently relate the proposed expenditures as given in the estimates to the policies declared by the Minister. Since the votes generally describe the nature of the expenditures and the detailed estimates are in the form of objects, the introductory statement is supposedly to inform the House of departmental policies and objectives. In the subsequent deliberations the Minister is required to steer his estimates through and clarify expenditures on which any questions are raised. But such informative direction on the part of Ministers is not always forthcoming. Even in regard to general departmental policies and objectives, curious parliamentary members have frequently expressed dissatisfaction with the Ministers' attempts at clarification. A typical reaction is the following comment by an opposition parliamentary member on the introductory statement of the Minister of Fisheries when he introduced the expenditure estimates for his department for the fiscal year 1963-64:

I was interested in listening to the introductory remarks of the Minister. They seemed to be composed mostly of a recitation of statistics and screenings from various departmental publications that had been issued over the years, especially this past year. When it came to an announcement of any definite policy that the fisheries department expected to promote, or what the government hoped to accomplish by its fisheries policy, we found the minister's speech just as barren as many of the fish-hooks of the fishermen when they pull them from the water.

.....

I think we could enunciate some of the objectives, some of the goals which the department and the minister should have in mind.⁵⁶

Following the introductory statement, consideration is given to Vote 1, the administration of the department. Here the discussion is usually fairly general with emphasis on government policies and the problems that relate to the general function of the department. For example, with regard to the Department of Transport, discussion may range from purely local matters such as grade crossings at Lac Megantic and grain handling facilities in Vancouver harbour to broad national issues

⁵⁶ Debates, October 24, 1963, p. 3973.

such as air policy and the operations of Air Canada, the merchant navy, communications in the country, etc. With the introduction of following votes the discussion reverts to the specifics of a department's existing and proposed operations. Many of the comments and questions pertaining to these votes are concerned with what the government is doing in these areas or what the government should be doing and are fairly time consuming. Equally time consuming, or perhaps more so, are the drawn out speeches presented by members in the cases where an expenditure concerns their constituencies or if they believe that the activity giving rise to the expenditure should be extended to areas within their constituencies. While no individual member of Parliament may move an increase in any vote, he may press for a policy change which, if accepted, would lead to an increase in an appropriation through later supplementary estimates.

The manner in which expenditure estimates are processed in Parliament has basically undergone little change since Confederation. In the early years following Confederation expenditures totalled approximately twelve to fifteen million dollars per year. In the current fiscal year they have reached the seven billion dollar mark. Yet Parliament is handling expenditures today in practically the same way as in those early years. They are still presented on the basis of objects with individual vote items having to be processed through the Committee of Supply. There has been much dissatisfaction with this procedure and rumblings of discontent can be found in parliamentary discussions dating well into the past. For instance, in 1933 one member of Parliament stated:

Is it any wonder that the Canadian people are today critical of our methods when they see millions and tens and sometimes hundreds of millions of dollars voted without any legitimate, honest or competent scrutiny as to where the money was going or whether it was being properly spent in conformity with the policies of this country.⁵⁷

In 1963 a revision of parliamentary treatment of estimates was still being sought:

...the time has come when we ought to be trying to find some way to improve our handling of these estimates.⁵⁸

And in 1964 the disenchantment with the presentation of estimates by objects of expenditure continued. During the consideration by Parliament of the 1964-65 estimates of the Department of Agriculture a few revealing comments were made by parliamentary members expressing their dissatisfaction with the form in which estimates were presented. The principal complaint was the lack of information regarding what was being done by the department for the benefit of agriculture or what the objectives of the department were. The following excerpts from speeches of members of the House serve to illustrate the dissatisfaction with the present form of estimates:

⁵⁷ Ibid., February 15, 1932-33, p. 2124.

⁵⁸ Ibid., July 15, 1963, p. 2192.

According to vote 15, there are 418 employees working for the Department of Agriculture. To do what? To hand out subsidies. And how much? . . . To whom?⁵⁹

.

I...confine my remarks to vote 15, but I do not see anything there for the farmers, all we can see is:

Salaries and wages	\$800,000
Overtime	1,700

.

Travelling and removal expenses	63,000
---------------------------------	--------

.

...in item 15 as in the whole budget for the Department which amounts to \$140 million, only 20% goes to farmers, the rest going to civil servants. But what is the function of those people?⁶⁰

.

...let us have some clear indications as to how the money is spent and not just the distribution of salaries....Let us have facts.⁶¹

And the reply of the Minister of Agriculture:

...I can appreciate that the way the various items are documented probably presents a problem in understanding them...⁶²

Standing Committee On Estimates

During its consideration of the expenditure estimates Parliament may refer the estimates of various departments to the Parliamentary Standing Committee On Estimates or other committees for a more thorough examination. The idea of a committee on estimates took form at the turn of the century and though it was proposed and discussed on several occasions it was not until 1955 that a special committee on estimates was established by the House of Commons. In 1958 the special committee was replaced by a standing committee consisting of sixty members. This committee only examines those estimates which are referred to it by the House. It is not, however, the only parliamentary standing committee which examines estimates, for the expenditures of certain departments may be referred to other committees as well, such as the Standing Committee on Veterans Affairs or the Standing Committee on External Affairs.

⁵⁹ Ibid., July 10, 1964, p. 5332.

⁶⁰ Ibid., p. 5333.

⁶¹ Ibid., p. 5338.

⁶² Ibid.

At the time that the first estimates committee was established in 1955, Parliament was devoting from one-fifth to one-third of its time to the consideration of estimates. The proponents of the committee believed that it would serve a two-fold purpose: first, parliamentary time would be saved in that there would be less time spent in Committee of Supply on expenditure details, and second, members would be given more opportunity to "cross-examine" individual Ministers and consequently become better informed of a department's operations.⁶³ Being thus better informed they could, it was believed, offer more constructive criticism and discussion in the Committee of Supply.

The Standing Committee on Estimates in an advisory committee only, for it remains the function of the Committee of Supply to decide whether expenditure items are to be approved. It was created as a fact finding committee which was to review departmental expenditure proposals in detail and to report to the House. In the process of this review the committee may order the attendance of the Minister of the department and his senior departmental officials for the purpose of giving evidence regarding departmental administration and operation. The difference between the present Standing Committee and the earlier Special Committee is that the present Committee is empowered to send for persons, papers, and records and summon outside witnesses. During its meeting in 1958 the Committee engaged in much heated debate on a motion to bring in outside persons, but the motion was finally defeated.⁶⁴ The consensus of opinion among committee members was that to bring in outside witnesses would result in the consideration of government policy which was not the purpose of the committee. In the words of one member:

...it is the duty of the government to recommend to us estimates, and in the consideration of the estimates we should examine the Minister and any officials of the department whom he wants to bring with him. It would serve no good purpose to bring outsiders....⁶⁵

There is no fixed procedure followed by the Standing Committee in its examination of estimates. The Committee is left to decide for itself as to how it shall proceed, but generally the procedure is similar to that in the Committee of Supply. The estimates of a department are reviewed vote by vote with members raising questions in regard to the activities and expenditures represented by these votes.⁶⁶ The result is a fairly detailed review of the operations of departments. A certain amount of

⁶³Debates, February 8, 1955, pp. 937-938.

⁶⁴Canada, House of Commons, Standing Committee On Estimates, Minutes of Proceedings and Evidence, July 15, 1958, pp. 440-444.

⁶⁵Ibid., p. 443.

⁶⁶As an illustration of the line of questioning followed consider the following excerpt from the proceedings of the Committee when it examined the estimates of the Department of National Health and Welfare in 1960:

"Indian and Northern Health Services Item No. 247, Operation and Maintenance including grants to hospitals and other institutions which

attention is also devoted to the objects of expenditure and the reasons for any change in personnel or in expenditure by object from the previous year, (e.g. reasons for increased expenditure for travel, telephones, etc. in any particular branch of a department). Furthermore, besides the examination of expenditure proposals, the committee serves the purpose of enabling parliamentary members to become informed of the intricacies of administration such as the line of work performed by different classes of public servants, the procedure in purchasing, the letting of contracts, etc.

On the basis of the past proceedings of the Standing Committee on Estimates it appears that the value of this review is primarily of an informative nature.⁶⁷ Parliament still finds itself pressed for time in its consideration of estimates. The Committee has not achieved any economies in expenditures, for it has yet to recommend a reduction in the estimates of a department. This is not surprising, however, for expenditure items are reasonably well screened by the Treasury Board and detailed search for economies by the Committee would no doubt end in small results in any event. Furthermore, in such a review of projects, items, and objects as is conducted by the Committee, there is a tendency to lose sight of the general objectives and programs of the department. Unless these activities, projects, and items are appraised in the context of the broader programs and objectives of which they are components, a review cannot be effectively conducted from the point of view of the necessity of the projects, the progress of the program,

care for Indians and Eskimos - - - - - \$21,362,102

MR. WINCH, [Member of Parliament] On the question of payments to hospitals, is that on a contract basis, or do you pay the going rate of the hospital?

DR. MOORE, [Director of Indian and Northern Health Services] Mr. Chairman, in each instance we negotiate a rate with the hospital. This is more particularly applicable now to sanatoria, because practically all the Indians are insured. In any province where insurance is in effect the Indians are insured, and we have arranged the payment of premiums.

MR. WINCH: How do you do it in a case like the province of British Columbia, where there is no premium rate, and it is all based on the sales tax?

DR. MOORE: We pay nothing except the co-insurance.

MR. WINCH: You say you pay nothing except the co-insurance. That is \$1 a day. Your department pays nothing beyond that \$1 a day? Is that on the basis that the Indians buy the same as everybody else and, therefore, they are paying on a 5 percent sales tax?

DR. MOORE: When premiums were in effect we paid the premiums for them, but when the premium was abolished the Indian pays the sales tax and is entitled to the same benefits."

See Ibid., April 26, 1960, pp. 342-344.

⁶⁷ For a critical evaluation of the Standing Committee On Estimates, see Norman Ward, "The Committee On Estimates," Canadian Public Administration, VI (1963), pp. 35-42.

or end products in terms of the objectives.

A more objective and thorough examination of departmental programs and expenditure estimates may be conducted by a small Parliamentary Committee rather than by a committee of the whole House, (e.g. the present Standing Committee on Estimates may request additional supporting data and may summon witnesses to give evidence). Furthermore, past experience of committees has indicated that generally the members of the committee sometimes tend to forget political aspects or party lines and concentrate objectively on the issue before them. The Standing Committee on Estimates, however, has not met since 1960. Presumably it has ceased to meet because it has not adequately fulfilled the purpose for which it was created. In the past the Committee would examine the estimates of one or more departments during the fiscal year, report to the House, and the House in turn would go through the estimates all over again as the Committee of Supply. While it is apparent that the estimates did receive a more thorough scrutiny by the Standing Committee than by the Committee of Supply, there was considerable duplication in this process. Conceivably a Committee on Estimates could be established with the function of examining in detail certain programs of several departments every year. The Committee could be required to submit precise and detailed reports to the House which in turn would consider the reports rather than examining once again the programs and estimates which have been examined by the Committee.

In May 1965 a motion was introduced in the House of Commons for changes in the Parliamentary rules governing the consideration of estimates. It was proposed that the detailed examination of estimates be undertaken by Standing Committees. In respect to the allocation of time it was proposed that not more than thirty days of the time of the House be allocated to the business of supply in each session. The "business of supply" was to consist of main estimates, interim supply, and supplementary or additional estimates excepting supplementary or additional estimates introduced after the main estimates have been approved.⁶⁸

The Public Accounts Committee

The final examination by Parliament of government financial transactions is conducted by the Standing Committee on Public Accounts which presently consists of fifty members. This committee was established in 1867⁶⁹ but has met rather infrequently. In recent years its meetings have become more regular, and since 1958 it has been chaired by a member from the leading party in opposition in Parliament.

⁶⁸The motion and its amendments were agreed to on June 8, 1965. See Debates, June 8, 1965, p. 2121.

⁶⁹For a history of the Public Accounts Committee see Norman Ward, The Public Purse (Toronto: University of Toronto Press, 1964), and H.R. Balls, "The Public Accounts Committee," Canadian Public Administration, VI (1963), pp. 15-34.

The Committee was established to assist the House of Commons to discharge its responsibility of financial control. The House found insufficient time to exercise its powers of detailed control and consequently delegated these functions to a standing committee of the House. Very broad terms of reference have been granted to the Committee. During its proceedings in which it examines the report of the Auditor General and the Public Accounts it may review almost any aspect of government finance and administration. The Public Accounts Committee, like the Committee on Estimates, is empowered to summon before it such witnesses as the Auditor General, the Comptroller, and the Ministers and officials of departments, and to call for documents.

The starting point of the review by the Standing Committee is generally the report of the Auditor General. This report deals with government financial operations by subject matter, and the transactions it draws to the attention of Parliament may range from the general to the very particular. For example, the 1962 report of the Auditor-General brought to the attention of Parliament such issues as Unemployment Insurance Administration, National Defence administrative regulations and procedures, expenditures incurred without Treasury Board approval, Veterans hospitals and institutions, examination of claims under the winter works program, renovation of a remote transmitter station in Halifax,⁷⁰ etc. In the consideration of such matters by the Public Accounts Committee the Auditor General is invariably present and usually elaborates on these matters further, following which the appropriate Minister and departmental officials are called upon for explanations.

⁷⁰The following excerpts are from the 1962 Auditor General's Report and serve to illustrate the matter brought to the attention of Parliament by the Auditor General:

"70. Examination of claims under the Winter Works Program. In last year's report...attention was drawn to the fact that, unlike most federal-provincial cost-sharing agreements, the agreements under which the federal government reimburses municipalities, through their provincial governments, for one-half of the direct payroll costs incurred on municipal winter works projects contained no specific provision for examination by federal officers of provincial or municipal records supporting the claims, the agreements providing for audit of the claims only by Provincial Auditors.

Officers of the Department of Labour have advised us that they will recommend the incorporation of a provision for examination by federal officers into future agreements submitted for consideration of the provinces and that, in the meantime, the provincial governments have been requested to make available for examination by the Auditor General, records pertaining to the 1962-63 program.

.....

78. Renovation of remote transmitter station, Halifax. In January, 1961, a contract for \$229,330 was awarded by the Department of Defence Production for renovation of antennae and transmission lines at an Air Force station near Halifax. The site test drawings indicated the

The Public Accounts Committee reports the results of its deliberations to the House of Commons for consideration by the House. The Treasury Board also conducts a study of the Committee's reports. In this respect, H.R. Balls has commented:

...the Treasury Board studies the reports, paragraph by paragraph, and asks departments to take action or to justify their lack of action on the Committee's recommendations. Either the Auditor General or a representative of the department concerned reports to the Committee at a subsequent session the action taken in implementing the Committee's recommendations or, if no action has been taken, the reasons why.⁷¹

Summary

In general, the budgetary system reflects the division of powers in the government between the Cabinet and the House of Commons. The Cabinet is responsible for the preparation and execution of the budget while the House of Commons is responsible for authorization and review. The Treasury Board, a committee of the Privy Council, assists the Cabinet in discharging its financial responsibilities and is consequently second only to the Cabinet in its capacity as a policy-making and expenditure-control body. The Department of Finance is responsible for analyzing economic conditions in the country, for economic and revenue forecasting, and for determining revenue policies.

Accountability to Parliament has been emphasized in the federal budget system, and in this respect various procedures have been established to insure that expenditure and revenue proposals are carried out as authorized and that Parliament receives a full accounting of the administration of public funds. Revenues are deposited in the Consolidated Revenue Fund from which payments are made under the direction and control of the Comptroller of the Treasury on the basis of Parliamentary appropriations. Parliament receives a full accounting in regard to financial transactions through the Auditor General.

bedrock to be from two to fourteen feet below the surface. However, during excavation the contractor discovered that the bedrock was from eighteen to twenty-five feet below the surface in many places....a complete redesigning of both the layout of foundations and their method of construction was required, and the contract was amended to provide for the additional costs of \$287,326 which resulted.

Attention is drawn to this expenditure because the contract was amended to an amount more than double that originally called for."

See Canada, Report of the Auditor General To The House of Commons for the Fiscal Year Ended March 31, 1962, p. 25 and 31.

⁷¹H.R. Balls, "The Public Accounts Committee," Canadian Public Administration, VI (1963), pp. 24-25.

Government expenditures are classified by objects of expenditure. It is on this basis that departments prepare their submissions of estimates to the Treasury Board and on which the Board conducts its annual expenditure review. This classification scheme, which serves as the basis of the expenditure allotments, appears to have been developed primarily for purposes of expenditure control. But control and accountability are not the only purposes that financial accounts are required to serve. There are the equally important purposes of decision-making with respect to the allocation of resources and of economic analysis. The present system, based on tradition, is quite out-moded and inadequate from this point of view.

The expenditure review by the Treasury Board and Parliament places considerable emphasis on the detailed objects of expenditure. In its review the Treasury Board has tended to rely primarily on past trends and to focus attention on incremental expenditures. One of the major deficiencies in this review is the lack of appropriate criteria for determining priorities among expenditure proposals. Parliamentary expenditure examination and appropriation procedures are likewise outdated as they have undergone little change since Confederation despite the tremendous expansion of government expenditure.

There is, however, considerable evidence of changes currently being instituted in the budgetary system, in respect to the expenditure side of the budget, as a result of the Glassco Commission's recommendations. This is particularly true of the process within departments. There is evidence of expenditures being planned on the basis of programs and activities, with some departments developing five-year expenditure plans and making use of these formal planning documents for compiling their estimates. The Commission strongly advocated less detailed control over departmental operations by such central control organizations as the Treasury Board and the Comptroller of the Treasury, and studies have been conducted regarding the feasibility of this. The Treasury Board has also been reorganized to a certain degree. While no noteworthy changes have recently been made in the form of the estimates, other than the consolidation of the estimates, or in the expenditure review process, changes can be anticipated in the near future.

APPENDIX E

STANDARD COMMODITY CLASSIFICATION, SERVICE CLASSIFICATION, AND STANDARD INDUSTRIAL CLASSIFICATION

TABLE E-I

STANDARD COMMODITY CLASSIFICATION*

List of Divisions

Division
Code

Section I - Live Animals

00 Live Animals

Section II - Food, Feed, Beverages and Tobacco

01 Meat and Meat Preparations
 03-04 Fish and Marine Animals
 05 Dairy Produce, Eggs and Honey
 06 Grain, Flour, Meal and Cereal Preparations
 07 Fruits and Fruit Preparations
 08 Nuts (exc. oil nuts)
 09 Vegetables and Vegetable Preparations
 10 Sugar and Sugar Preparations
 11 Cocoa, Coffee, Tea and Spices
 12 Margarine, Shortening and Lard
 14 Miscellaneous Foods, Food Materials and Food Preparations
 15 Fodder and Feed (exc. unmilled cereals)
 17 Beverages
 18 Tobacco

Section III - Crude Materials, Inedible

20 Crude Animal Products, Inedible (exc. fibres)
 21 Crude Vegetable Products, Inedible (exc. tobacco, fibres
 and wood)
 23 Crude Wood Materials
 24 Textile and Related Fibres (incl. waste)
 25 Metals in Ores, Concentrates and Scrap
 26 Coal, Crude Petroleum and Related Crude Products
 27 Crude Non-Metallic Minerals (exc. coal and petroleum)
 29 Waste and Scrap Materials, n.e.s.

Section IV - Fabricated Materials, Inedible

30 Leather
 31 Furs, Dressed
 32 Rubber Fabricated Materials
 33 Wood Fabricated Materials
 34 Pulp
 35 Paper and Paperboard
 36-38 Textile Fabricated Materials
 39 Oils, Fats, Waxes, Extracts and Derivatives, Animals and
 Vegetable
 40-42 Chemicals and Related Products
 43 Petroleum and Coal Products

TABLE E-I -- Continued

Division
Code

44	Iron and Steel and Alloys
45	Non-Ferrous Metals
46	Metal Fabricated Basic Products
47	Non-Metallic Mineral Basic Products
49	Miscellaneous Fabricated Materials

Section V - End Products, Inedible

50-55 Machinery

50	General Purpose Industrial Machinery
51	Conveying, Elevating and Materials Handling Equipment
52	Special Industry Machinery
54	Agricultural Machinery and Implements (exc. tractors)
55	Tractors

57-63 Transportation and Communication Equipment

57	Railway Rolling Stock
58	Road Motor Vehicles
59	Ships and Boats
60	Aircraft
61	Miscellaneous Vehicles
62	Rubber Tires and Tubes
63	Communication and Related Equipment

65-77 Other Equipment and Tools

65	Heating, Air Conditioning and Refrigeration Equipment
66	Cooking Equipment for Food
67	Plumbing Equipment and Fittings
68	Electric Lighting, Distribution and Control Equipment
69	Other Electric Equipment and Appliances
70	Measuring, Controlling, Laboratory, Medical and Optical Instruments, Apparatus and Accessories (exc. X-ray equipment)
71	X-ray and Related Equipment
72	Safety and Sanitation Equipment; Alarm and Signal Systems
73	Service Industry Equipment (incl. vending machines)
74	Furniture and Fixtures
75	Hand Tools and Cutlery (exc. table and kitchen)
76	Other Equipment
77	Office Machines and Equipment

78-86 Personal and Household Goods

78	Apparel and Apparel Accessories (exc. footwear)
79	Footwear
80	Toiletries, Cleaning Preparations and Household Chemical Specialities

TABLE E-I -- Continued

Division
Code

81	Jewellery and Silverware (exc. watches and clocks)
82	Watches and Clocks
83	Recreation Equipment, Toys, Games, Sporting and Athletic Goods, n.e.s.
84	House Furnishings
85	Kitchen Utensils, Cutlery, and Tableware (exc. silverware)
86	Miscellaneous Household and Personal Equipment
87-96	<u>Miscellaneous</u>
87	Medicinal and Pharmaceutical Products
88	Medical Supplies, Ophthalmic Goods, Orthopaedic Appliances
89	Printed Matter
90	Stationers' and Office Supplies and Artists' Materials
91	Photographic Goods
92	Musical Instruments
93	Firearms, Weapons and Ammunition
94	Miscellaneous Products
95	Containers and Closures
96	Remaining End Products, Classified by Material

List of Divisions and Groups
in SCC

<u>Division Code</u>	<u>Group Code</u>	<u>Section I - Live Animals</u>	<u>Number of Groups Classes</u>	
00		<u>Live Animals (00)</u>	7	42
	00 1	Cattle		7
	00 2	Sheep		2
	00 3	Swine		2
	00 4	Horses		3
	00 6	Poultry		8
	00 7	Fur-bearing animals		8
	00 9	Other live animals		12
		<u>Section II - Food, Feed, Beverages and Tobacco (01-18)</u>		
01		<u>Meat and Meat Preparations</u>	4	55
	01 1	Meat, fresh, chilled or frozen		15
	01 3	Meat, cured		12
	01 5	Ready-cooked meat and meat preparations, not canned		10
	01 7	Meat and meat preparations, canned		18

TABLE E-I -- Concluded

<u>Division Code</u>	<u>Group Code</u>		<u>Number of Groups</u>	<u>Classes</u>
03-04		<u>Fish and Marine Animals</u>	12	200
	03 1	Fish, whole or dressed, fresh or chilled		43
	03 3	Fish, whole or dressed, frozen		28
	03 5	Fish, filleted, fresh or chilled		20
	03 7	Fish, filleted, frozen		21
	03 9	Fish blocks and fish sticks		7
	04 1	Fish, smoked or salted and smoked		12
	04 2	Fish, salted and/or dried		12
	04 3	Fish, pickled		13
	04 4	Fish, canned		17
	04 6	Shellfish		22
	04 8	Meat of marine animals		1
	04 9	Other fishery foods and feeds		4
05		<u>Dairy Produce, Eggs and Honey</u>	3	46
	05 1	Dairy produce		36
	05 3	Eggs		9
	05 5	Honey		1
06		<u>Grain, Flour, Meal and Cereal Preparations</u>	6	54
	06 1	Cereals, unmilled		13
	06 2	Cereals, milled		15
	06 4	Bakery products, incl. frozen		11
	06 5	Macaroni products		4
	06 6	Cereal products		5
	06 9	Farinaceous substances and flour for use as food		6

*Source: Dominion Bureau of Statistics, Standard Commodity Classification Manual (Ottawa: Queen's Printer, 1959).

TABLE E- II

SERVICE CLASSIFICATION*

Service Division Code	Service Division
0	<u>Personnel Compensation</u>
00	Civil salaries and wages
01	Civilian allowances
02	Pay and allowances, Defence Forces and R.C.M.P.
03	Pensions, superannuation and other benefits in consideration of personnel services - civil
04	Pensions, superannuation and other benefits in consideration of personnel services - military and R.C.M.P.
1	<u>Transportation</u>
10	Transportation of persons
11	Transportation of things (except by mail)
12	Parcel post
2	<u>Communication</u>
20	Postage (except parcel post)
21	Telephone
22	Telegraph, cable and wireless communication
23	Other communication services (courier, etc.)
3	<u>Real Estate Service</u>
30	Real estate rental
31	Other real estate service (management, appraisal, etc.)
4	<u>Education Services</u>
40	Education, elementary, secondary and special (incl. vocational)
41	Education, university and college
5	<u>Health and Welfare Services</u>
50	Hospital Service
51	Other health services
52	Welfare service
6	<u>Business Services</u>
60	Motion pictures production and distribution
61	Photography service except motion picture

TABLE E-II -- Concluded

Service Division Code	Service Division
62	Advertising service
63	Accountancy service
64	Banking services
65	Bond and investment services
66	Legal services
67	Engineering and scientific services
68	Protective service (Corps of Commissionaires, etc.)
69	Other Business services
7	<u>Personal Services</u>
70	Laundry, dry cleaning and related services
71	Hotel service
72	Restaurant service
73	Other lodging and food services
74	Other personal services
8	<u>Repair and Maintenance Service</u>
80	For structures
81	For vessels
82	For aircraft
83	For vehicles
84	For other equipment
9	<u>Miscellaneous Services</u>
90	Services to buildings (char service, window washing, etc.)
91	Rental of equipment
92	Storage and warehousing
93	Other services

*With the exception of the Division Code this classification is one which has been developed by the Dominion Bureau of Statistics.

TABLE E-III

STANDARD INDUSTRIAL CLASSIFICATION

List of Divisions and Groups

Code	
<u>Division</u>	<u>Group</u>
1	<u>Agriculture</u>
	1 Experimental and institutional farms
	2 Small Agricultural holdings
	3 Commercial farms
	4 Services incidental to agriculture
2	<u>Forestry</u>
	1 Logging
	2 Forestry services
3	<u>Fishing and Trapping</u>
	1 Fishing
	2 Fishery services
	3 Hunting and trapping
4	<u>Mines, Quarries and Oil Wells</u>
	1 Metal mines
	2 Mineral fuels
	3 Non-metal mines except coal mines
	4 Quarries and Sand Pits
	5 Services incidental to mining
5	<u>Manufacturing Industries</u>
	1 Food and beverage industries
	2 Tobacco products industries
	3 Rubber industries
	4 Leather industries
	5 Textile industries
	6 Knitting mills
	7 Clothing industries
	8 Wood industries
	9 Furniture and fixture industries
	10 Paper and allied industries
	11 Printing, publishing and allied industries
	12 Primary metal industries
	13 Metal fabricating industries (except machinery and transportation equipment industries)

TABLE E-III -- Concluded

<u>Division</u>	<u>Group</u>
	14 Machinery industries (except electrical machinery)
	15 Transportation equipment industries
	16 Electrical products industries
	17 Non-metallic mineral products industries
	18 Petroleum and coal products industries
	19 Chemical and chemical products industries
	20 Miscellaneous manufacturing industries
6	<u>Construction Industry</u>
	1 General constructors
	2 Special trade contractors
7	<u>Transportation, Communication and Other Utilities</u>
	1 Transportation
	2 Storage
	3 Communication
	4 Electric power, gas, and water utilities
8	<u>Trade</u>
	1 Wholesale trade
	2 Retail trade
9	<u>Finance, Insurance and Real Estate</u>
	1 Financial institutions
	2 Insurance and real estate industries
10	<u>Community, Business and Personal Service Industries</u>
	1 Education and related services
	2 Health and welfare services
	3 Religious organizations
	4 Motion picture and recreational services
	5 Services to business management
	6 Personal services
	7 Miscellaneous services
11	<u>Public Administration and Defence</u>
	1 Federal administration
	2 Provincial administration
	3 Local administration
	4 Other government offices
12	<u>Industry Unspecified or Undefined</u>

Source: Dominion Bureau of Statistics, Standard Industrial Classification Manual (Ottawa: Queen's Printer, 1960).

APPENDIX F

THE USE OF INTER-INDUSTRY FLOWS IN TRACING THE EFFECTS OF CHANGES IN FINAL DEMAND : MATHEMATICAL REVIEW

Problems involving inter-industry flows are most conveniently stated using matrix algebra. The following makes use of elementary properties of matrices in tracing the effects on industries of a change in final demand for the product of a given industry.¹

TABLE F-I

Inter-industry Flows

		Purchasing Industry Intermediate Use						Final Demand	Total Supply
		1	2	.	.	.	n	Households (incl. gov't)	
Producing Industry	1	x_{11}	x_{12}	.	.	.	x_{1n}	x_1	X_1
	2	x_{21}	x_{22}	.	.	.	x_{2n}	x_2	X_2

	n	x_{n1}	x_{n2}	.	.	.	x_{nn}	x_n	X_n
Primary inputs (labour)		M_1	M_2	.	.	.	M_n		Y

Assume that there are n industries in which the value of the product of the i th industry is denoted by X_i . This product is used by other industries as intermediate products and also goes to final demand which includes households and government, conveniently shown as one sector. Let x_{ij} represent the amount of the product of the i th industry used by the j th industry, and let x_i represent the amount passed on to final demand. It follows that

$$X_1 = x_1 + x_{11} + x_{12} + \dots + x_{1n}$$

or

$$X_i = x_i + \sum_{j=1}^n x_{ij} \quad \begin{matrix} (i = 1, 2, \dots, n) \\ (j = 1, 2, \dots, n) \end{matrix} \quad (1.1)$$

¹This presentation borrows heavily from R.G.D. Allen, Mathematical Economics (London: McMillan & Co., 1956), pp. 343-370; H.B. Chenery and P.G. Clark, Interindustry Economics (New York: Wiley & Sons, 1959), pp. 13-53; Richard Stone, Input-Output And National Accounts (Paris: The Organization

For convenience, the primary input has been lumped together as one factor — labour. Summing this input over industries we have

$$Y = \sum_{i=1}^n M_i \quad (1.2)$$

In inter-industry analysis it is assumed that the input coefficients are fixed. If a_{ij} is the amount of x_i required in the production of 1 dollar of product in the j th industry, then

$$x_{ij} = a_{ij} X_j \quad (1.3)$$

Similarly,

$$M_j = b_j X_j \quad (1.4)$$

where b_j represents the value of the primary input required in the production of 1 dollar of output in industry j .

The matrix of input coefficients may be derived from the transactions matrix. Since $a_{ij} = \frac{x_{ij}}{X_j}$, the matrix of input coefficients may be found

by dividing X_j down the j th column. Similarly $b_j = \frac{M_j}{X_j}$.

In a three industry case the output equations would be:

$$\begin{aligned} X_1 - (a_{11}X_1 + a_{12}X_2 + a_{13}X_3) &= x_1 \\ X_2 - (a_{21}X_1 + a_{22}X_2 + a_{23}X_3) &= x_2 \\ X_3 - (a_{31}X_1 + a_{32}X_2 + a_{33}X_3) &= x_3 \end{aligned} \quad (1.5)$$

Excluding intra-industry consumption, $x_{ij} = 0$ and $a_{ij} = 0$ where $i = j$, and the technology matrix is:

$$A = \begin{bmatrix} 1 & -a_{12} & -a_{13} \\ -a_{21} & 1 & -a_{23} \\ -a_{31} & -a_{32} & 1 \end{bmatrix} \quad (1.6)$$

For European Economic Co-operation, 1961), pp. 73-83; and University of Cambridge, Department of Applied Economics, A Programme For Growth, Input-Output Relationships 1954-1966, ed. Richard Stone (London: Chapman and Hall, 1963).

Solving for outputs (X_1, X_2, X_3),

$$X_1 = \frac{1}{D} (A_{11}x_1 + A_{21}x_2 + A_{31}x_3)$$

$$X_2 = \frac{1}{D} (A_{12}x_1 + A_{22}x_2 + A_{32}x_3)$$

$$X_3 = \frac{1}{D} (A_{13}x_1 + A_{23}x_2 + A_{33}x_3)$$

where D represents the determinant obtained from A , and A_{ij} represents the co-factors of A . Total primary input follows from equations (1.2) and (1.4).

$$Y = b_1X_1 + b_2X_2 + b_3X_3$$

The effects on production and primary input of a change in the final demand for the product of Industry 1, other final demands remaining constant, is shown as:

$$\frac{\partial X_1}{\partial x_1} = \frac{A_{11}}{D}; \quad \frac{\partial X_2}{\partial x_1} = \frac{A_{12}}{D}; \quad \frac{\partial X_3}{\partial x_1} = \frac{A_{13}}{D}$$

and

$$\begin{aligned} \frac{\partial Y}{\partial x_1} &= b_1 \frac{\partial X_1}{\partial x_1} + b_2 \frac{\partial X_2}{\partial x_1} + b_3 \frac{\partial X_3}{\partial x_1} \\ &= \frac{1}{D} (b_1A_{11} + b_2A_{12} + b_3A_{13}). \end{aligned}$$

Y is in value terms. To derive employment in physical terms, divide the average annual wage in each industry into the total value of primary input into that industry. If w_i is the average wage in industry i , then employment in that industry will be

$$\frac{b_1X_1}{w_1}$$

and total physical manpower employed in the three industry case is

$$\frac{b_1X_1}{w_1} + \frac{b_2X_2}{w_2} + \frac{b_3X_3}{w_3}.$$

The change in total output resulting from a change in final demand may similarly be calculated by use of the inverse matrix. The output equations (1.5), in matrix form become

$$X - AX = x$$

To carry out the subtraction, multiply X by the identity matrix. This gives

$$IX - AX = X(I - A) = x$$

which is equivalent to

$$\begin{bmatrix} (1-a_{11}) & -a_{12} & -a_{13} \\ -a_{21} & (1-a_{22}) & -a_{23} \\ -a_{31} & -a_{32} & (1-a_{33}) \end{bmatrix} \begin{bmatrix} X_1 \\ X_2 \\ X_3 \end{bmatrix} = \begin{bmatrix} x_1 \\ x_2 \\ x_3 \end{bmatrix}$$

The matrix $I-A$ becomes the technology matrix shown in (1.6) since $a_{ij} = 0$ where $i = j$.

From $X(I-A) = x$ we have

$$\begin{aligned} X &= x(I-A)^{-1} \\ &= x(I + A + A^2 + A^3 + \dots) \end{aligned}$$

The matrix inverse of the form $(I-A)^{-1}$ is termed the matrix multiplier on analogy with the conventional multiplier $\frac{1}{1-b}$ where b denotes the marginal propensity to consume. In order to meet the final demand, x , the productive system must produce $Ix = x$, the final outputs themselves; Ax the direct inputs into the final outputs; $A^2x \equiv A(Ax)$, the inputs into the direct inputs, and so on in a convergent infinite series. Therefore the element in row i and column j of the matrix $(I-A)^{-1}$ represents the direct and indirect requirements of the output of industry i needed to produce one unit of output in industry j .

In regard to primary input,

$$Y = b_1X_1 + b_2X_2 + b_3X_3$$

which in matrix form becomes,

$$\begin{bmatrix} M_1 & M_2 & M_3 \end{bmatrix} = \begin{bmatrix} b_1 & b_2 & b_3 \end{bmatrix} \begin{bmatrix} X_1 \\ X_2 \\ X_3 \end{bmatrix}$$

and

$$\begin{aligned} Y &= BX \\ &= Bx (I-A)^{-1} \end{aligned}$$

Using this equation the change in the primary input resulting from a change in final demand can be determined.²

²For a discussion on methods for computing the inverse matrix, see H.B. Chenery and P.G. Clark, Interindustry Economics (New York: Wiley & Sons, 1959), pp. 50-53.

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